DOJ OVERSIGHT: *U.S.* v. *A.T.&T.*

HEARINGS

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

FIRST AND SECOND SESSIONS

ON

THE DEPARTMENT OF JUSTICE OVERSIGHT OF THE UNITED STATES VERSUS AMERICAN TELEPHONE AND TELEGRAPH LAWSUIT

AUGUST 6, 1981, AND JANUARY 25, 1982

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DOJ OVERSIGHT: *U.S.* v. *AT&T*

THURSDAY, AUGUST 6, 1981

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The committee met, pursuant to notice, at 10:15 a.m., in room 2228, Dirksen Senate Office Building, Senator Strom Thurmond (chairman of the committee) presiding.

Staff present: Peter Chumbris, senior counsel for antitrust; Marcy J. K. Tiffany, counsel for antitrust and chief economist; and W. Stephen Cannon, chief counsel for antitrust.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The CHAIRMAN. The committee will come to order.

On July 29, 1981, the Justice Department requested that the Federal district court grant an approximate 1-year continuance in the case of *United States* v. *American Telephone & Telegraph.* The Department was joined in its request by A.T. & T. At the time this request was made, the Government had completed presenting its case against A.T. & T. and the defense was scheduled to begin presenting its case the following Monday, August 3.

In seeking the continuance of the lawsuit, both the Government and A.T. & T. cited their desire to give telecommunications legislation now pending before the full Senate a chance to become law. If this legislation became law within a year, the parties noted there would be no need to resume the trial and the case could be dismissed. Shortly after this request was made, it was denied by district court Judge Harold Greene.

The significance of this lawsuit is difficult to overstate. Likewise, a decision to postpone, dismiss, or otherwise affect the lawsuit is equally significant and is appropriately the subject of congressional scrutiny. I would note that following the termination of the Government's 1946 lawsuit against A.T. & T. by a consent decree in 1956, the House Judiciary Committee conducted an extensive investigation of that settlement.

The committee was not pleased with the actions of the Government in that case. In its report to the Congress, the committee noted that:

> Upon all the evidence adduced in the committee's investigation, the consent decree entered in the A.T. & T. case stands revealed devoid of merit and ineffective as an instrument to accomplish the purposes of the antitrust laws.

The committee further noted that:

> The decree not only failed to effectuate the purposes of the Sherman Act but was arrived at without adequate consideration of the issues by those responsible for the protection of the Government's interests.

As we begin this hearing today, our committee expresses no opinion on the actions of the administration in regard to the current lawsuit against A.T. & T., some 25 years after the 1956 consent decree was entered. Our purpose is to examine the facts behind the decision to seek a postponement of the case.

It must be pointed out, however, that the administration appears to have clearly and inextricably tied together the fate of the lawsuit with that of the telecommunications legislation now pending in the Congress. This committee has, of course, exhibited an active interest in S. 898, the Telecommunications Deregulation and Competition Act of 1981, citing antitrust concerns raised by the bill.

Over the past few weeks we have held 5 days of hearings on telecommunications antitrust problems. This action by the administration serves only to heighten the interest of the committee in this area and illustrates the importance of the antitrust implications in the legislation.

Before we proceed, I would note that the importance of this matter dictated that a hearing be held as soon as it was practicable. Unfortunately, the Senate is now in recess and consequently numerous committee members must be absent to fulfill commitments in their home States. I want to assure those absent committee members that the record will remain open for a reasonable period of time, and they will be given a full opportunity to submit written questions to these witnesses.

Today we are fortunate to have three distinguished members of the administration to discuss the events of the past week. Our first witness is Hon. Malcolm Baldrige, Secretary of Commerce, incidentally not only an able Secretary but an expert professional cowboy. Mr. Secretary, on behalf of the committee, I want to welcome you.

These matters are important, and as we take them up we will ask the witnesses to be sworn, if you will raise your right hand.

Do you swear that the evidence you will give in this hearing shall be the truth, the whole truth, and nothing but the truth, so help you God?

Secretary BALDRIGE. I do.

The CHAIRMAN. Secretary Baldrige, you may now proceed with your statement.

TESTIMONY OF HON. MALCOLM BALDRIGE, SECRETARY OF COMMERCE, ACCOMPANIED BY SHERMAN UNGER, GENERAL COUNSEL; AND BERNARD WUNDER, ASSISTANT SECRETARY FOR COMMUNICATIONS AND INFORMATION

Secretary BALDRIGE. Thank you very much, Senator. I am pleased to be here this morning, and thank you for the opportunity. I would like to discuss the bill briefly first, if I may, because that is an important part of our consideration today.

With me this morning are Sherman Unger, on my right, the Department's General Counsel; and Bernard Wunder, our Assistant Secretary for Communications and Information, on my left. They

are fully prepared to address the specifics of any detailed questions that the committee may have.

The administration strongly supports passage of S. 898. We believe that this bill is fundamentally sound and that the industry needs an updated law. With the amendment dealing with A.T. & T.'s procurement and sales activities that we are now recommending, and perhaps an amendment dealing with section 207, S. 898 will provide a sound framework for the future competitive development of this important industry. This amendment has our full support and is a result of efforts of the Cabinet Council to resolve cross-subsidy concerns.

A special task force to study the telecommunications industry and the implications of S. 898 was appointed at White House direction. The task force reviewed recent competitive developments affecting the telecommunications industry as well as critical national defense, security, and emergency preparedness needs.

The recommendations of this task force were submitted promptly to the Cabinet Council on Commerce and Trade, of which I serve as Chairman. Subsequently, the Justice Department recommended administration endorsement of a further, "special open-market and procurement" amendment that addresses A.T. & T.'s current product procurement and sales practices.

The Justice Department had two principle concerns in the area of cross-subsidy which it did not believe were adequately addressed by S. 898. First, much of the domestic market for telecommunications products is foreclosed to competitors of Western Electric. Second, there is no effective marketplace check on prices for which Western Electric transfers products to affiliated firms.

The absence of any effective marketplace test concerning intrafirm transfer prices gives rise to two concerns. First, the Bell System operating companies may pay excessively high prices for the products that they use to provide regulated telecommunications service. Second, cross-subsidies between competitive and noncompetitive product lines are possible.

The amendment to S. 898 that the Justice Department developed has as its major effect the establishment of a marketplace check on internal Bell System transfer prices. The amendment also should substantially lessen the market foreclosure problem, should Western Electric prove to be an inefficient producer.

If in any given period Western Electric proves unable to sell its products on the open market, for cost or for other reasons, the operating companies themselves would be required to cut back on their purchases of Western Electric equipment. Other independent producers would then supply operating company needs.

Another important aspect of the proposed amendment is that it would reinforce existing incentives for A.T. & T. to market products abroad more aggressively. In short, the practical effect of the proposed amendment would be to create competition while at the same time fostering international trade.

The President considered the recommendations of the Cabinet Council on S. 898 and related matters, as well as the proposed amendment advanced by the Justice Department. His determination was that the administration should support S. 898, if the bill were amended to include the Justice Department's special open

market amendment and a strengthening of section 207 of the bill, which pertains to interconnection services provided by A.T. & T. We plan to work affirmatively with Congress to develop any further amendments to S. 898 that may be needed.

The Reagan administration strongly supports congressional efforts to reform our telecommunications laws. We believe it would be preferable by far for the Congress, and not the Federal courts, to strike the balance among sometimes competing and conflicting concerns. Competition is our fundamental national economic policy.

Insuring a strong national defense, however, is an equally fundamental national commitment. We also wish to insure that the legitimate needs and interests of rural Americans are protected, and it is critical that we seek at this time to foster expanded world trade, especially in high-growth, high-technology sectors such as telecommunications, where we still have the lead.

In short, as former Attorney General Griffin Bell observed in his testimony before the Senate Commerce Committee on S. 898, issues of the magnitude and importance as the role and structure of the Nation's telecommunications industry are best resolved by Congress.

In conclusion, the administration strongly supports the prompt enactment of S. 898, and we urge that the open market amendment proposed by Justice be adopted. We will continue to work on the important issue of system interconnection, and expect to be able to present administration recommendations on this topic soon.

As we have already promised you, Mr. Chairman, and the committee staff, we will also work with your committee to insure that this legislation is the best possible product. We need significant revision of the 1934 act; few would disagree with that. The task at hand is to produce a piece of legislation that promotes competition, deregulates whenever possible, protects the national defense, is fair to all, and puts the U.S. industry in the best possible position to compete both at home and abroad.

Thank you, sir. I will be glad to answer any questions you may have.

The CHAIRMAN. Thank you, Mr. Secretary.

Mr. Secretary, I have several questions, and I am going to give you the liberty of answering them yourself or, if you would prefer having your counsel answer some of the questions.

Secretary BALDRIGE. Thank you, sir.

The CHAIRMAN. Mr. Secretary, who gave the specific directive that a task force be established to study the telecommunications industry?

Secretary BALDRIGE. As you know, Senator, the Commerce Department through NTIA has the job of coordinating the administration's policy on telecommunications. We have been working on that for some 4 months, since last April.

On May 20, I and my General Counsel met with the President's chief counselor, Mr. Meese, to review impediments to the enactment of reform telecommunications legislation. On May 28, the counselor to the President established the task force which the Commerce Department chaired, to ascertain and advise the President—this was our charge—as to the present state of the telecom-

munications industry and what our national policy in regard to that should be.

The CHAIRMAN. Was a directive given to you in writing, and if so, by whom was it signed?

Secretary BALDRIGE. Yes, sir, the directive was given in writing to me by the President's chief counselor, Mr. Meese.

The CHAIRMAN. Who was requested to participate in the task force?

Secretary BALDRIGE. On the task force were the agencies or departments that had the closest concerns with national telecommunications policy, our overall policy, and what the administration's position should be. This was the Defense Department, the Agriculture Department, the Energy Department, the Federal Emergency Management Agency, and the Commerce Department.

Those were the agencies represented on the task force. They are the ones with the closest concern with our overall telecommunications policy in the administration.

The CHAIRMAN. Who made the determination as to who would be invited to participate?

Secretary BALDRIGE. As I remember, sir, that was decided in the meeting with the President's counselor, myself, and I am not sure who else was there but essentially we made those decisions.

The CHAIRMAN. Since the Department of Justice has an Antitrust Division and is responsible for enforcing the law, I was just wondering why the Department of Justice was not invited.

Secretary BALDRIGE. I do not think, sir, that we felt other than that the Justice Department was charged with legal matters, antitrust matters, and so forth. This task force was not in any way to address the merits of the case, the pending case. The task force was to decide, or make recommendations for the President to decide what the administration's policy should be as far as our national interest went. The Justice Department had a more narrowly defined function, that of prosecuting the laws.

The CHAIRMAN. Was there a working group established by the task force, and if so, when was the group established?

Secretary BALDRIGE. The working group was established on May 28 or 29. We had the agencies represented that I have just mentioned to you. A background paper was produced that they signed off on, and the next step was to take this paper to the Cabinet Council on Commerce and Trade.

The CHAIRMAN. Who were the members of the working group?

Secretary BALDRIGE. Well, the agencies and bureaus that I have just mentioned, sir: Defense, Agriculture, Energy, Federal Emergency Management Agency, and Commerce.

The CHAIRMAN. Were there any written instructions given to the working group by the task force?

Secretary BALDRIGE. Just the letter that I had mentioned earlier, the directive from the President's chief counselor, Mr. Meese, asking the working group to look into the present state of the telecommunications industry and make recommendations as to wherein our national interests lay, so that the administration could get its policy position ready.

The CHAIRMAN. Who were the individual members of the working group?

Secretary BALDRIGE. Well, the Commerce people were the gentlemen on my right and left here, General Counsel Unger and Assistant Secretary Wunder. I do not remember, Senator, the other individual members of the committee.

The CHAIRMAN. Would you like to consult with Mr. Unger? Maybe he could tell you, or you could answer, Mr. Unger, if you know.

Secretary BALDRIGE. Yes. Go ahead.

Mr. UNGER. The other members of the working group were the General Counsels of the respective Departments, except the General Counsel of the Department of Energy had to recuse himself and ultimately an Assistant Secretary joined the working group, I believe Assistant Secretary Heffelfinger. I would need to check my records.

The CHAIRMAN. Would you check and supply the names for the record at this point?

Mr. UNGER. I would be pleased to.

[The following material was subsequently supplied for the record:]

MEMBERS OF THE WORKING GROUP OF THE TASK FORCE ON TELECOMMUNICATIONS POLICY

Sherman E. Unger, General Counsel, Department of Commerce.
A. James Barnes, General Counsel, Department of Agriculture.
William H. Taft, IV, General Counsel, Department of Defense.
Thomas C. Newkirk, Deputy General Counsel for Regulation, Department of Energy (Attended the June 4 meeting. He subsequently recused himself and was replaced by William S. Heffelfinger, Assistant Secretary, Management and Administration, Department of Energy).
George Jett, General Counsel, Federal Emergency Management Agency.

The CHAIRMAN. Was there a task force of the Secretaries and a working group of the lower echelon?

Secretary BALDRIGE. Well, if you want to call the General Counsels lower echelon, Senator; I would not like to see them described that way. I thought it was pretty high echelon.

The CHAIRMAN. We will call it "others." [Laughter.]

Secretary BALDRIGE. I would call that a relatively high echelon, at least in my opinion.

The CHAIRMAN. However, the task force did consist of the Secretaries?

Secretary BALDRIGE. The task force itself had a working group made up of the individuals, the General Counsels and so forth, that we will supply you later. The Secretaries all had to read and concur with the efforts of that working group but it was like an interagency group, and the Secretaries were advised and could either concur or not with the recommendations of their representatives on that group.

The CHAIRMAN. How often did the working group meet?

Secretary BALDRIGE. I think the working group itself met, what, once, twice?

Mr. UNGER. The working group met as a working group one time, though we distributed a study and papers prior to the meeting for review by the working group. Then there were discussions afterward on certain amendments and changes but we had one formal meeting.

Secretary BALDRIGE. Senator, the working group had been supplied with a rather extensive background paper to work from that Commerce had the lead on and had been preparing for some time.

The CHAIRMAN. Could you supply for the record the dates that the working group met? Mr. Unger, could you supply that?

Mr. UNGER. Yes, we could do that.

Secretary BALDRIGE. Yes, we will be glad to.

[The following was subsequently supplied for the record:]

The meeting of the Working Group was held on June 4, 1981.

The CHAIRMAN. Did the working group submit any written reports to the task force?

Secretary BALDRIGE. Yes.

The CHAIRMAN. Did the task force or the working group conduct any studies designed to ascertain the present state of the telecommunications industry?

Secretary BALDRIGE. Yes.

The CHAIRMAN. Would you describe them?

Secretary BALDRIGE. Essentially, the product of the working group addressed the present state of the telecommunications industry, the present state of the pending legislation, the possibilities of legislative action being effective in this session, and made recommendations based on their findings there.

I would like to ask Assistant Secretary Wunder if he has any other important issues that I have failed to mention.

Mr. WUNDER. The only additional items that I would mention, Senator, would be foreign trade issues and questions of the status of competition in the United States in the telecommunications industry.

The CHAIRMAN. Were any written reports of such studies prepared?

Secretary BALDRIGE. I am sorry, Senator. I did not hear you.

The CHAIRMAN. Of the underlying studies, were there any reports prepared, any written reports?

Secretary BALDRIGE. Essentially there were two papers: There was the working paper that I mentioned before, that was reviewed by the task force, and then the task force recommendations.

The CHAIRMAN. Mr. Secretary, how often has the task force met since its formation?

Secretary BALDRIGE. The task force physically met once to review the paper that I have described. Then, after the meeting and their recommendations, this matter was moved up to the Cabinet Council on Commerce and Trade.

The CHAIRMAN. Mr. Secretary, were all the members of the task force present at the meeting of the task force?

Secretary BALDRIGE. I would have to defer——

The CHAIRMAN. You can answer that for the record, if you would prefer, Mr. Unger.

Secretary BALDRIGE. Yes. I want to differentiate between the two. The working group—the interagency group, what I am used to calling the task force—after the meeting and after they made their recommendations, then I called all of the Secretaries or the heads of the agencies involved to make sure that they concurred before we took this to the Cabinet Council on Commerce and Trade.

We did that on June 12. On June 12 the Cabinet Council on Commerce and Trade, with the President in attendance, met to consider the task force's recommendations, so it was moved to that forum on June 12. At that meeting, besides taking up the task force recommendations, Senator, the Justice Department was included so that their concerns could be fully voiced.

If you would like, sir, I can describe in general the product of the task force, what this report was about, if it would be of interest.

The CHAIRMAN. I think that would be helpful.

Secretary BALDRIGE. We were asked to look at the state of the industry and address wherein our national interests lay.

What we found out—because we looked not just at the state of the industry in the United States but the state of the industry worldwide, because that is going to affect us in the next two decades—we found that the telecommunications industry and the computer industry are rapidly converging on a worldwide basis. We found that as far as international leadership went, it was one of the few industries left where we still, as the United States, are world leaders.

We found that the Japanese, Germans, and other countries are trying to take that lead away from us. As a matter of fact, in the case of Japan, they have deliberately targeted one of their companies to take over world leadership from IBM in the next 10 years. They are subsidizing their industry heavily in order to do so, protecting it in order to do so. Therefore, we found an intense worldwide competition and a convergence of the telecommunications and the computer industries, so that they will be more or less indistinguishable in the next 20 years.

We found that the U.S. industry was working under a 46-year-old Communications Act, and also under a 24-year-old consent decree. They were being sued under an 83-year-old Antitrust Act based on facts assembled on the state of the industry as of a decade or so ago. I think it is very important to note that this industry is in no way, shape, or form the same that it was at the time of the 1934 Communications Act.

I can remember, as I have testified before, using a crystal set and a pair of earphones when I was a kid in 1934. I can remember going down to the telegraph office to watch the Morse code being tapped out. Now we have fiber optics, satellite systems, and microwave. We found in this task force that the state of the art in the industry had leapfrogged itself so many times that it was imperative to deregulate and make this competitive if we were not going to relinquish leadership to other countries in the future.

Therefore, this led us to the conclusion that it was vital to have the Congress settle these very important problems rather than the judicial forum, which was a much narrower forum. This is too important for that because it affects everybody in the United States. It should be decided by the branch of the Government that is closest to the people, after full and fair hearings.

We also felt that in the judicial chambers we would not get adequate representation of the views because there was no way to get these views expressed, the Defense Department's concern—they had some very important concerns—Agriculture, Energy, Federal Emergency Management Agency, and the Commerce Department's

concerns about international leadership in this field drifting away from us unless we could update the act.

We felt that it had been shown that it was almost—I will not say impossible—but almost impossible for an updated, modern act on telecommunications policy to get through the Senate and the House both with the antitrust suit against A.T. & T. hanging over their heads. That was a real deterrent. It has been tried twice before and has not worked.

Therefore, we did not in any way address the merits or the content of the A.T. & T. suit but we did recognize the fact that the suit was holding up some vitally needed legislation. We felt it was in the national interest to recommend to the President that we pursue the congressional course and not the judicial course.

I think there is another point, Senator, before I leave that whole area. Part of our job in the Commerce Department in getting an administration policy or leading an administration policy in this area, is and has been talking to the people in the industry and hearing firsthand what their problems are. I am talking about the competitors of A.T. & T.

We found widespread belief that because of the uncertainty surrounding the antitrust suit and what would happen in Congress, that for some years now vitally needed new product developments, investment in research and development that we need to keep abreast of the rest of the world, and financing was not available to some of these companies. We were holding back, by lack of action in Congress, we have been holding back the development of one of the most important industries in the United States of America. That is why we made the recommendations we did, not on the merits of the case at all.

The CHAIRMAN. Mr. Secretary, don't you think that the concerns of the Justice Department regarding the competitive structure of the industry were also important in making telecommunications policy?

Secretary BALDRIGE. Well, as I said before, sir, I think that they of necessity and rightfully have to take a narrower approach in their specialized area than our particular charge was. We were asked what was in the overall national interest and to look into the state of the industry, which really meant worldwide, as far as I was concerned, because we cannot call this just a domestic industry right now.

Senator, we did recognize the role of the Justice Department as a voice by including them in the Cabinet Council, when the Cabinet Council on Commerce and Trade first addressed this issue. The Justice Department was represented there, had a chance to speak up and voice their concerns with the President of the United States in attendance. Therefore, we feel they had a full and fair hearing.

The CHAIRMAN. With regard to your decision not to include the Justice Department in the task force, isn't it fair to say that whatever decisions the task force made could significantly affect the *A.T. & T.* case?

Secretary BALDRIGE. Yes.

The CHAIRMAN. You do not think it was appropriate to include the Justice Department——

Secretary BALDRIGE. Well, Senator, when we——

The CHAIRMAN [continuing]. Along with all of the others in preparing the task force report?

Secretary BALDRIGE. Senator, excuse me. When we discovered in the working group that the antitrust case was a major impediment to getting legislation through the Congress, when the task force made its findings that the antitrust case was one of the major impediments to getting new legislation through the Congress, then we did include them in the Cabinet Council, which is a higher body than the task force. They were represented there and spoke up there.

The CHAIRMAN. What specific recommendations did the task force report make?

Secretary BALDRIGE. The task force went into the items I have just mentioned and recommended that the case be dismissed because, with the case pending, we did not feel that we could get the legislation through Congress that we needed so badly. That was the recommendation of the task force.

Now the Cabinet Council on Commerce and Trade, with the President in attendance, when they considered that recommendation every member of the Cabinet Council was directed, at that meeting on June 12, to develop comments on this recommendation, to develop proposed amendments that might take care of it. We made the decision to meet again to consider those recommendations and potential amendments before any decision was made on the recommendations, so we met again on July 15, about a month later.

The CHAIRMAN. Who are the members of the Cabinet Council on Commerce and Trade?

Secretary BALDRIGE. The Secretary of Commerce is the Chairman. The members—and I know I am going to forget some because I am doing this from memory—are the Secretary of——

The CHAIRMAN. You may supply those for the record, if you would prefer to do it.

Secretary BALDRIGE. I would like to because I would hate to miss somebody. It was the Secretary of Treasury—there are four or five and I will supply that for the record.

[The material was subsequently supplied for the record:]

CABINET COUNCIL ON COMMERCE AND TRADE

MEMBERS

Secretary of Commerce (Chairman Pro Tem), Malcolm Baldrige.
Secretary of State, Alexander Haig.
Secretary of Treasury, Donald T. Regan.
Attorney General, William French Smith.
Secretary of Agriculture, John R. Block.
Secretary of Labor, Raymond J. Donovan.
Secretary of Transportation, Andrew L. Lewis, Jr.
United States Trade Representative, Ambassador William E. Brock.
Chairman of the Economic Advisors, Murray L. Weidenbaum.

EX OFFICIO MEMBERS

Vice President, George Bush.
Counsellor to the President, Edwin Meese III.

The CHAIRMAN. Mr. Secretary, on what basis did the task force arrive at the conclusion that the legislation would be held up by the lawsuit?

Secretary BALDRIGE. I suppose, practical experience in the past. It had been tried through two different Congresses, and had never gotten out. It was the opinion of a good many Congressmen and Senators whose opinion we respected that that had been the major impediment. We had seen the testimony of Attorney General Bell, Griffin Bell, when the Justice Department came down and supported the bill in the last administration and Congress still could not get a bill out.

Therefore, we were very bothered by that, Senator. Here is an industry that clearly needs up-to-date congressional legislation to restructure it, after 46 years, after two Congresses had not been able to get it out with the Attorney General in support of it. Therefore, we saw no other course to take but what we did. This is vitally important to this country, for our national defense effort among other things, that we get legislation on this. Otherwise we are going to be buying telecommunications equipment and electronics from the Japanese in 10 years.

The CHAIRMAN. Mr. Secretary, did the task force consult any Members of Congress in reaching the conclusion that legislation would not be enacted unless the suit was either suspended or dismissed? If so, who was consulted, and what views did they express?

Secretary BALDRIGE. I do not remember all of them.

The CHAIRMAN. Senators or House members.

Secretary BALDRIGE. I do not remember all of the people, Senator, but obviously Senator Packwood, Congressman Broyhill, and I think Senator Baker. I do not remember all of the rest of them. It was to get a feeling.

I would say that was part of the process but I think the more important thing was that we had all seen this tried twice before in the Congresses, and the idea of having this Congress go by without addressing that and coming out with a bill would have meant another 2 years. We just do not have that time if we are going to compete in the future.

The CHAIRMAN. Did you consult or did the task force consult any Member of Congress concerned with antitrust matters?

Secretary BALDRIGE. I do not remember, sir.

The CHAIRMAN. I do not recall having been consulted myself, and I wondered if you consulted any other members concerned with antitrust in the Senate or the House.

Secretary BALDRIGE. No, sir, I do not remember any. Let me just say that probably we did not because the antitrust suit itself, as I have mentioned before, the merits of this suit were not at issue. We did not get into the merits of this suit.

I know this is hard to say in front of the Judiciary Committee chairman in a room full of lawyers but the merits of this suit were not at issue at all. We did not care about the merits of this suit. We are talking about the national interest here; that is of overriding importance, and we thought it was. We did not address the merits of the suit at all.

The CHAIRMAN. I suppose competition is part of the national interest?

Secretary BALDRIGE. Yes, sir, but getting up-to-date rules of competition in the world of today is impossible with a 46-year-old law. We are talking about having the Congress decide, as the closest body to the people, rather than a single judge in a forum someplace deciding it. We thought that was the best way to go.

The CHAIRMAN. Mr. Secretary, has the administration reached a final decision not to seek dismissal or further suspension of the lawsuit pending passage of telecommunications legislation by this Congress?

Secretary BALDRIGE. As you know, sir, the administration asked for a continuance and that was turned down. That is the position we are in now. I think it would be inappropriate for me to speculate on what the administration's position would be if Congress did not pass a telecommunications act this session. I just do not know but right now the matter is in the hands of Congress and the judge has turned down a continuance.

The CHAIRMAN. Mr. Secretary, I believe you mentioned that you were not concerned about the antitrust matters in the case. How about the antitrust aspects of S. 898?

Secretary BALDRIGE. Yes, sir, we are very concerned about that. We feel, as I have stated before, that this matter should be decided by the branch of the Government that is closest to the people, after full and fair hearings. Therefore, I would expect that after the Senate hearings and after the House hearings on the bill, that every concerned part of the constituency will have had a chance to be heard and that Congress will vote on the appropriate legislation to take care of those concerns.

However, that is a much broader field of concerns being heard, a much broader spectrum of concerns being heard than is allowed in the judicial chambers. There is no way for the Defense Department to testify before a judge, no way for the Federal Emergency Management Agency to testify before a judge. There is no way for me as Secretary of Commerce to testify before a judge and tell him what is happening in telecommunications throughout the world and what is happening to our leadership as a result of lack of moving ahead in this legislative arena.

The CHAIRMAN. I believe you said that no Members of Congress were consulted concerning the antitrust phase of the suit. Were any Members of Congress consulted concerning the antitrust aspects of S. 898?

Secretary BALDRIGE. Yes. We discussed——

The CHAIRMAN. If so, what Members of Congress were consulted?

Secretary BALDRIGE. Our working group was not addressing for this purpose—you know, for the purpose of their recommendations—the antitrust part of the amendment. We felt, Senator, that that should be left to the Congress. We were not pretending in any way, shape, or form to shape the congressional bill as far as antitrust matters went. We felt that should be left to the Congress after full and fair hearings and that the Congress should write in the antitrust provisions that they wanted.

We did support, as an administration, the general thrust of the bill; and we did support and do support, as an administration, the Justice Department's chief concern with the bill, as a result of which they brought up the amendment that I mentioned earlier.

Therefore, those parts were addressed but we felt the Congress should decide those matters.

The CHAIRMAN. There is no question in your mind that S. 898 does involve antitrust implications?

Secretary BALDRIGE. Oh, no, sir. Of course it does.

The CHAIRMAN. There is no question about that?

Secretary BALDRIGE. There is no question about that, and there is no question that Congress is the best forum in which to decide that. We are in agreement.

The CHAIRMAN. Well, I just wondered if you might not have felt it advisable, then—if S. 898 does contain antitrust implications—to have consulted with those concerned with antitrust matters in the Congress before committing to the bill?

Secretary BALDRIGE. Well, Senator, the job of the working group was not to really express an opinion one way or the other on the antitrust part of the bill. The job of the working group was to, in essence, come out with a recommendation: Do we need a bill or don't we? How important is it to the national interest? What is holding it up?

We felt it was the job of Congress to address the antitrust parts of the bill, as in any other part of the bill. What we are saying essentially is, please, we need a bill. Let the Congress decide——

The CHAIRMAN. Wouldn't it be helpful to you, then—since S. 898 does contain antitrust implications—to consult with those who are concerned with antitrust matters in the Congress because this bill does concern those of us who are interested in antitrust matters?

Secretary BALDRIGE. Yes, sir.

The CHAIRMAN. If you had consulted with us, maybe we could have helped you some.

Secretary BALDRIGE. Yes, sir. Well, I will certainly say that that statement could be very correct, and I will do my best from now on. I cannot undo what has gone before.

The CHAIRMAN. In the transcript of the proceedings before Judge Greene, Mr. Trienens, the attorney for A.T. & T., indicated it was his understanding that if S. 898 were enacted into law by this Congress that the antitrust lawsuit against A.T. & T. would be dismissed. Is this in fact the position of the administration?

Secretary BALDRIGE. It was the position of the administration in seeking the continuance, that if the continuance were granted, that if appropriate legislation were passed, there would be in the administration's view no need to continue this suit because the chief concerns of the Justice Department have been addressed by the amendment that they have proposed.

The CHAIRMAN. Is this currently their position?

Secretary BALDRIGE. No. Our current position is, we recommended that to—we asked the judge for that. He turned it down. We feel that the matter is in the hands of Congress now, and our position now is to work with—as you have suggested, Senator, more closely, perhaps—with the Senate and the House to do everything the administration can to get the proposed legislation through.

The CHAIRMAN. Is it now the administration's position that if the bill passes the suit will be dismissed?

Secretary BALDRIGE. No, sir. We do not want to speculate.

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The CHAIRMAN. You would prefer not to answer that at this time?

Secretary BALDRIGE. We just do not want to speculate, really, on what would happen because we do not know really in what form—we do not know if a bill is going to be passed, we do not know what form it will take, we do not know how the Congress will vote, and I think it is inappropriate to speculate now on what would happen until it has happened.

The CHAIRMAN. You see, Mr. Secretary, the administration has sponsored a bill in the Congress involving the biggest corporation in America, which is bound to contain competitive aspects and is bound to bring about a consideration of the antitrust matters involved. It is really surprising, since it does involve antitrust, that the people in the Congress responsible for antitrust matters were not even consulted, not only about the suit but also about this legislation.

Secretary BALDRIGE. Well, if you take the legislation, Senator, this was not a bill brought up by the administration. This bill came up through the Senate and I had assumed that you were consulted in the Senate about the provisions of the bill.

The CHAIRMAN. No. This bill was brought out by the Commerce Committee, and it does have serious antitrust questions involved. We requested the bill be referred to the Judiciary Committee so the antitrust lawyers and myself and others concerned with antitrust aspects of it could study it to determine if it is best for the public. That is our only interest.

Secretary BALDRIGE. Yes, sir.

The CHAIRMAN. We have no desire to slow up any legislation but we have a responsibility to look after the interests of the public. The request that we made to refer it to the Judiciary Committee was never answered. I made the request to the chairman of the Commerce Committee and he never did reply to my letter. Twice we made the request.

That is the reason we are holding hearings on the telecommunications industry, to determine if there are antitrust implications in this bill that need to be addressed. We have three expert lawyers here on antitrust matters. They are all well-qualified and we feel that this committee should have had this bill for, say, 30 days to study it and possibly then send it out, maybe with no recommendations or maybe with some recommendations for amendments.

Since that was not done, then the recourse left to us was to hold hearings and determine if amendments are needed; to consider the amendment that has been agreed upon between the Government and the A.T. & T.; and to consider what other amendments are needed. That is the purpose of these hearings.

Secretary BALDRIGE. Yes, sir, I understand.

The CHAIRMAN. It would have been helpful if the antitrust people had been consulted, and maybe we could have suggested—maybe before the bill was introduced, or consulted with us afterwards as to what amendments were needed, if any. As I say, we only desire to protect the public interest. We do have a responsibility to do that, and that we expect to do.

Secretary BALDRIGE. Yes, sir. I suppose that, rightly or wrongly, we had viewed that as a jurisdictional matter within the Senate, about where the bill was to be heard, and—

The CHAIRMAN. Well, it really should be considered by both committees because it is a commerce matter and, at the same time, it involves antitrust. Frequently bills are considered by both committees. Here it is our duty to determine if we feel that amendments should be offered to protect the public. That is what we want to do here.

Secretary BALDRIGE. Yes, sir.

The CHAIRMAN. We want to consider the amendment that you all have agreed to concerning the equipment, and then we want to consider interconnection amendments if any are needed, and maybe some other aspects.

I guess you were not aware of the request we made to refer the bill. Of course, you did not have control over that but I——

Secretary BALDRIGE. No. I have only been in Washington 6 months, Senator, but I have learned not to get into jurisdictional disputes in the Congress, and I did not think that was appropriate for us.

The CHAIRMAN. No, I am not suggesting you do that.

Secretary BALDRIGE. Thank you.

The CHAIRMAN. Has the administration committed to supporting an amendment to S. 898 to deal with the interconnection problems in the industry?

Secretary BALDRIGE. Yes, sir. The amendment, the details of the amendment have not been worked out yet, at least as of today, but we support the idea of working out an amendment that would take care of any possible problems on interconnection.

The CHAIRMAN. I believe you did work out with A.T. & T. the amendment on the equipment.

Secretary BALDRIGE. Well, that was the Justice Department and A.T. & T. That was a question of the Justice Department's concerns, major concerns with the antitrust suit, in prosecuting it.

The CHAIRMAN. Anyway, that has been worked out, I understand, with the approval of the Justice Department, on the equipment——

Secretary BALDRIGE. Yes.

The CHAIRMAN. And that amendment is being supported by A.T. & T. and the Government, too, as I understand it.

Secretary BALDRIGE. No, no. It is not being supported by A.T. & T., now. It is being supported by the Government.

The CHAIRMAN. I understood they had agreed to that amendment.

Mr. UNGER. No, Senator, they said it was technically workable.

The CHAIRMAN. What was that?

Mr. UNGER. They said it would work. They did not agree to it and did not commit to support it.

The CHAIRMAN. They did not agree to go along with that amendment?

Mr. UNGER. They did not agree to support it, and I understand they are opposing it today.

The CHAIRMAN. Now on the interconnections, are you working on an amendment now to submit to the Congress?

Mr. UNGER. The Justice Department is drafting a proposed amendment. We will review it in Commerce. I would presume we will present it to A.T. & T. to see if they think it is technically feasible. We are working on it but it will originate in the Justice Department.

The CHAIRMAN. Do you know whether the Justice Department and A.T. & T. had any understanding when there was a request for a continuance, concerning that amendment?

Mr. UNGER. You would have to ask them.

Secretary BALDRIGE. If I may say so, sir, I think that question is more properly answered by the Justice Department who are here today. I would rather have them——

The CHAIRMAN. Maybe your counsel would care to answer.

Mr. UNGER. Senator, we were very careful not to discuss the litigation when we met to talk about the legislation. Any discussions of the litigation were held at the Justice Department, between the Justice Department and A.T. & T. We did not participate, and I do not know of any arrangements that may or may not have been made. I am sure Assistant Attorney General Baxter can respond to that.

The CHAIRMAN. Is the administration prepared to support other amendments, besides the open market and interconnection amendments, that might be necessary to alleviate the antitrust concerns raised by the Antitrust Division and by this committee?

Secretary BALDRIGE. Absolutely, Senator. We cannot obviously say we would support every amendment that came up because we have not seen them yet but I think there will undoubtedly be other amendments that come up as a result of the hearings in the House, and perhaps these hearings here, and we would be prepared to either support or not support depending on how we viewed it.

The CHAIRMAN. Mr. Secretary, I understand that certain members of the press and private industry have somehow obtained copies of the task force report and certain other of the documents we have been discussing today. Is it possible for this committee to obtain a copy of the task force report, as well as copies of any supporting documents or studies prepared in support of that report, and also of the directive from Mr. Meese regarding establishment of the task force?

Secretary BALDRIGE. Well, I do not know, in the first place, that anybody has that task force report. I know that no one has gotten one from the Department of Commerce.

The CHAIRMAN. Has that been made public?

Secretary BALDRIGE. No, sir, not to my knowledge.

The CHAIRMAN. Well, I had better not go any further on that at this time.

Mr. Secretary, thank you very much. I know you are busy, and we will excuse you. I presume you would want to leave your lawyers here to hear what goes on, though. [Laughter.]

We appreciate your presence and thank you for your testimony.

Secretary BALDRIGE. Thank you very much, Mr. Chairman. I was glad to do it.

[Prepared statement follows:]

STATEMENT OF MALCOLM BALDRIGE

SECRETARY OF COMMERCE

Thank you for this opportunity to discuss the Reagan Administration's telecommunications regulatory reform efforts with you generally. With me this morning are Sherman Unger, the Department's General Counsel, and Bernard Wunder, our Assistant Secretary for Communications and Information. Mr. Unger and Mr. Wunder are prepared fully to address the specifics of any detailed questions that the Committee may have.

The Administration strongly supports passage of S. 898. We believe that the bill is fundamentally sound, and that the industry needs an updated law. With the amendment dealing with AT&T procurement and sales activities that we are now recommending and perhaps an amendment dealing with Section 207, S. 898 will provide a sound framework for the future, competitive development of this important industry. This instant amendment has our full support and is the result of the efforts of the Cabinet Council to resolve cross-subsidy concerns.

A special task force to study the telecommunications industry and the implications of S. 898 was empaneled at White House direction. The task force reviewed recent competitive developments affecting the telecommunications industry as well as critical national defense, security, and emergency preparedness needs.

The recommendations of this task force were submitted promptly to the Cabinet Council on Commerce and Trade, of which I serve as Chairman Pro Tem. Subsequently, the Justice Department recommended Administration endorsement of a further

"special open market and procurement" amendment that addresses AT&T's current product procurement and sales practices.

The Justice Department had two principal concerns in the area of cross-subsidy which it did not believe were adequately addressed by S. 898. First, much of the domestic market for telecommunications products is foreclosed to competitors of Western Electric. Second, there is no effective marketplace check on prices for which Western Electric transfers products to affiliated firms. The absence of any effective marketplace test concerning intra-firm transfer prices gives rise to two concerns. First, Bell System operating companies may be paying excessively high prices for the products that they use to provide regulated telecommunications services. Second, cross-subsidies between competitive and noncompetitive product lines are possible.

The amendment to S. 898 that the Justice Department developed has as its major effect the establishment of a marketplace check on internal Bell System transfer prices. The amendment also should substantially lessen the "market foreclosure" problem, should Western Electric prove to be an inefficient producer. If in any given period Western Electric proves unable to sell its products on the open market, for cost or other reasons, the operating companies themselves would be required to cut back on their purchases of Western Electric equipment. Other independent producers would then supply operating company needs. Another important aspect of the proposed amendment is that it would reinforce existing incentives for AT&T to market products abroad more aggressively. In short, the practical effect of the proposed amendment would be to create competition while, at the same time, fostering international trade.

The President considered the recommendations of the Cabinet Council regarding S. 898 and related matters, as well as the proposed amendment advanced by the Justice Department. His determination was that the Administration should strongly support S. 898, if the bill were amended to include the Justice Department's "special open market" amendment and a strengthening of Section 207 of the bill which pertains to interconnected services provided by AT&T. We plan to work affirmatively with Congress to develop any further amendments to S. 898 that may be needed.

The Reagan Administration strongly supports Congressional efforts to reform our telecommunications laws. We believe that it would be preferable for Congress, and not the Federal courts, to strike the balance among sometimes competing and conflicting concerns. Competition is our fundamental national economic policy. Ensuring a strong national defense, however, is an equally fundamental national commitment. We also wish to ensure that the legitimate needs and interests of rural Americans are protected; and it is critical that we seek at this time to foster expanded world trade, especially in high-growth, high-technology sectors, such as telecommunications. In short, as former Attorney General Griffin Bell observed in his testimony before the Senate Commerce Committee on S. 898, issues of the magnitude and importance as the role and structure of the nation's telecommunications industry are probably best resolved by Congress.

In conclusion, the Administration strongly supports the prompt enactment of S. 898, and we urge that the "open market" amendment proposed by the Justice Department be adopted. We will continue to work on the important issue of "system

interconnection" and expect to be able to present Administration recommendations on this topic soon. As we have already promised Senator Thurmond and the Committee staff, we will also work with your Committee to ensure that this legislation is the best possible product. We need significant revision of the 1934 Act, few would disagree with that. The task at hand is to produce a piece of legislation that promotes competition, deregulates whenever possible, protects the national defense is fair to all, and puts the United States industry in the best possible position to compete both at home and abroad.

The CHAIRMAN. Our next witness is Professor Baxter, the head of the Antitrust Division of the Justice Department.

Professor Baxter, do you have a statement you would like to make?

Mr. BAXTER. No, Mr. Chairman. I understood primarily that——

The CHAIRMAN. You had better hold up your hand and be sworn first.

Do you swear that the evidence you give in this hearing shall be the truth, the whole truth, and nothing but the truth, so help you God?

Mr. BAXTER. Yes.

TESTIMONY OF WILLIAM F. BAXTER, ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, U.S. DEPARTMENT OF JUSTICE

Mr. BAXTER. I understood that primarily you wished to ask questions, and I am here to answer them to the best of my ability.

The CHAIRMAN. All right. Professor Baxter, when did you first become aware that a task force had been formed within the administration to assess the feasibility of legislation to modify the structure of the telecommunications industry, and to make recommendations regarding the handling of the lawsuit against A.T. & T.?

Mr. BAXTER. I am not sure I can produce a calendar date, Mr. Chairman, but it was a day or two before the meeting of the Cabinet Council to which the Secretary of Commerce referred.

The CHAIRMAN. Were you or other representatives of the Justice Department requested to participate in the task force meetings?

Mr. BAXTER. No, sir.

The CHAIRMAN. When were you first informed that the administration was considering having the Justice Department request a suspension of the antitrust lawsuit, and by whom were you so informed?

Mr. BAXTER. Well, that simply was a compromise position that emerged from administration discussions subsequent to that Cabinet Council meeting. I could not—I think perhaps it was——

The CHAIRMAN. Did you participate in the Cabinet Council meeting?

Mr. BAXTER. Yes, Mr. Chairman, I did. I am the representative of the Justice Department on a number of issues but because the Attorney General and the Deputy Attorney General are recused on telecommunications problems, I have always been the Justice Department representative on the Cabinet Council with respect to those matters.

The CHAIRMAN. Professor Baxter, in your position have you encountered any difficulty in dealing with the other Cabinet officers on this matter?

Mr. BAXTER. Well, obviously there is a wide spectrum of points of view. If you mean, do people sometimes disagree with me and I with them, the answer is certainly yes. However, I do not regard that as an unexpected or unhappy difficulty.

The CHAIRMAN. What was your reaction to the decision to request a suspension of the antitrust lawsuit?

Mr. BAXTER. Well, since the alternatives seemed less attractive to me, I supported it. Indeed, I guess I urged it.

The CHAIRMAN. What were the alternatives?

Mr. BAXTER. Since it was the administration's conviction that the legislation could not be moved through the Congress while the case was pending, there was discussion of whether the case should be dismissed, or dismissed without prejudice, or merely suspended, and it seemed to me that suspending it was a preferable course.

The CHAIRMAN. Did the Justice Department have an opportunity to review or comment on the report of the task force in which the recommendation was made to dismiss the Justice Department lawsuit against A.T. & T., before that report was submitted to the administration?

Mr. BAXTER. Well, the report was distributed to the departments and agencies that are represented on the Cabinet Council on Commerce and Trade, of which the Justice Department is one, prior to the meeting of the Cabinet Council to which the Secretary of Commerce referred. I received it and saw it at that point in time, and we did prepare comments on it.

I attended the meeting of the Cabinet Council to which the Secretary has referred and urged that the matter be considered further. It was considered further, as the Secretary has indicated. The outcome of those considerations was, first, that the administration's support of S. 898 should include further amendments intended to address antitrust concerns, and, second, in order to expedite the movement of the legislation in the Congress, that an attempt should be made to seek what I call a continuance, what others have referred to as a suspension of the lawsuit.

The CHAIRMAN. Professor Baxter, do you know whether A.T. & T. had agreed to an amendment on equipment at the time a suspension of the lawsuit was requested by you?

Mr. BAXTER. I know the history of that amendment in great detail, Mr. Chairman. Whether there was an agreement with respect to the amendment is difficult to say. Certainly the A.T. & T. representatives participated extensively in the preparation of that amendment. I drafted it initially. We met with them because it affects some very technical matters and I was anxious to assure that there were no technical defects in it which I could not myself perceive.

Therefore, it was discussed with them, and redrafted. Their approval, as a precondition to administration support, was certainly never sought. I think they understood that they were there to be given an opportunity to provide technical assistance, but that their approval of the amendment as such was not being sought. Certainly that was my understanding.

The CHAIRMAN. I believe Secretary Baldrige indicated that the administration would support an amendment on the equipment but he seemed to not be certain whether A.T. & T. had agreed to go along with it. Have you had a chance to study that amendment on equipment, and could you give us your position on that?

Mr. BAXTER. Yes. I not only have had an opportunity to study it, I guess I would say I was its primary author. My comments in general are that there are several significant sources for possible cross-subsidization in the telecommunications industry, of which equipment sales to the basic operating companies—and indeed to the in-

terexchange network, so long as it continues to be regulated—is the primary source.

The amendment to which you are referring is an endeavor to prevent cross-subsidization arising from that source. What the amendment does, in essence, is to tell the Bell System that as a precondition to its selling any telecommunications equipment to its regulated affiliates, it must succeed in selling the very same items of equipment to unaffiliated enterprises in open and competitive markets.

If it is able to sell a particular type of switch successfully at a particular price in open and competitive markets, then it is able to sell that particular item of equipment to its regulated affiliates. Thus, a check is imposed on equipment quality and price to assure that there cannot be a supracompetitive flow of funds out of the regulated affiliates with which the phenomenon of cross-subsidization can be financed.

The CHAIRMAN. Professor Baxter, do you know whether the administration had committed itself to an amendment as part of the arrangement to dismiss the case—I am speaking about the amendment, now, on equipment—if the legislation were passed by Congress?

Mr. BAXTER. I am sorry, Mr. Chairman, I did not understand the question.

The CHAIRMAN. Do you know whether the administration had committed itself to support the amendment on equipment provided the legislation passed Congress?

Mr. BAXTER. Yes, the administration has committed itself to support that open-market equipment amendment, Mr. Chairman.

The CHAIRMAN. Would that be required before the case would be dismissed?

Mr. BAXTER. Well, that implies a connection between the passage of the legislation and dismissal of the case that I am not certain exists. However, I have no hesitancy whatsoever in suggesting that the administration has committed itself to support the open market equipment amendment, about which we have just talked, as an amendment to S. 898.

The CHAIRMAN. Now, S. 898 as it was introduced and passed the committee and is now before the Senate, does not contain this equipment amendment, does it?

Mr. BAXTER. It does not.

The CHAIRMAN. That is the amendment the Justice Department favors, and that is the amendment that we have been discussing here this morning.

Mr. BAXTER. Yes, one of several that we favor, Mr. Chairman.

The CHAIRMAN. What other amendments, Professor Baxter, do you favor to improve the bill as passed by the committee, the Commerce Committee?

Mr. BAXTER. The second amendment that has been discussed and which the administration has committed itself to support in principle is an amendment having to do with equal access by the competitive longlines companies—competitive interexchange carriers, in the phraseology of the bill—to interconnect with the regulated telephone companies. That amendment also is a very technical one.

There are problems because of the complexity of the switches at which the interconnection must occur, and the support is in principle only so far, precisely because technical language that would really implement the objective of affording equal quality access at equal cost to the competitive interexchange carriers has not yet been drafted. Therefore, there could not be commitment more than in principle. We are working on that drafting project, Mr. Chairman, and——

The CHAIRMAN. You are working on that amendment now——

Mr. BAXTER. Yes, sir.

The CHAIRMAN [continuing]. And the administration has committed to support it?

Mr. BAXTER. Yes, sir, but necessarily the commitment is less detailed in its articulation than with respect to the other amendment.

The CHAIRMAN. Would you care to mention any other amendments that you are working on, and which the administration will support, to this bill?

Mr. BAXTER. Those are the only two amendments that we are working on at present, Mr. Chairman. Those are the only two amendments that the administration conditions its support for S. 898 on at this time, and has affirmatively expressed a view that they should be in such legislation.

The CHAIRMAN. In other words, the administration, as I understand it, will insist on those two amendments that you mentioned, the equipment and the interconnection, and is committed to support those. Now are there any others that you are considering or will consider, to this legislation?

Mr. BAXTER. Well, I am sure the administration will consider any other amendments that this committee or, indeed, the Commerce Committee thinks would advance the objectives of creating a sound economic and technical structure for this enormously important industry over the years to come.

The CHAIRMAN. Professor Baxter, what does the term access line mean as it is used in one of those amendments?

Mr. BAXTER. Access line is a technical term that refers to the piece of wire that connects the individual telephone station with the local switching network. It is a measure of how many customers there are out there. Each customer in general represents one access line. There might be a number of extensions on that line but it would still only be one access line.

Therefore, as you will see, the phrase is used for the purpose of constructing a ratio and the notion is, by counting the number of access lines that a particular telephone company has, it is a measure of the company's market share or the extent of its participation in the industry. For example, A.T. & T. at the present time has about 80 percent of the Nation's access lines, which roughly translates into 80 percent of the Nation's customers.

The CHAIRMAN. Professor Baxter, why does the proposed amendment exclude from the access line ratio all carriers affiliated with the manufacture of telecommunications products?

Mr. BAXTER. Well, the notion there was that A.T. & T. would face perhaps unfair difficulties in attempting to sell its equipment to the telephone companies of General Telephone. General Tele-

phone has, I believe, about 8 percent of the Nation's access lines. However, General Telephone, like A.T. & T., is extensively vertically integrated and makes a large amount of its own telecommunications equipment.

General Telephone--to a much lesser extent, to be sure, but to some extent—has an incentive to prefer to buy from its own integrated supplier. We are asking A.T. & T. to go out and prove its equipment and to prove its prices in competitive markets. The notion was that extensively vertically integrated companies such as General Telephone did not represent a truly open, competitive market, and therefore they were excluded.

Now I must confess that phrase, which was quite hurriedly written—and one of the unhappy aspects of this to me is that so much has been done rather hurriedly—I think is broader than was really intended. The intended reference is to other substantially integrated companies that give rise to foreclosure problems of that kind.

The CHAIRMAN. Professor Baxter, I wonder if you would mind explaining the theory behind the amendment in plain English so the laymen could understand that?

Mr. BAXTER. Well, if we assume just for the purposes of this discussion that the world is a little simpler than in fact it is—and let's assume therefore that the A.T. & T. company has exactly 80 percent of the local telephone business, and that a group of independent carriers have the other 20 percent—if there were perfectly free and open competition in the supply of telephone equipment, any particular supplier would on average sell about 80 percent of his equipment to Bell operating companies and about 20 percent of his equipment to independent operating companies, just because Bell is four times as big.

All the complicated ratios that are talked about in that amendment boil down to saying this: They say to the A.T. & T. Co.:

> In order to maintain a 75 percent market share of the Bell operating companies' business, you must achieve 75 percent of the independent operating companies' business. In order to retain 50 percent of the Bell operating companies' business, you must achieve 50 percent of the independent operating companies' business.

Basically that is what those ratios dictate but, since the Bell market is four times as big as the independent market, that means that four times as many sales can occur in the Bell market as in the independent market. That is what the amendment provides.

Now that is not quite what the amendment provides. As I say, I started off oversimplifying a bit. Bell has the opportunity to sell in foreign markets where it has no competitive advantages, as well as to the independent market in the United States. Therefore, the amendment a little more accurately stated, says:

> For every $100 of equipment you sell, either to the independent market in the United States or to foreign markets, you may sell four times as much to the Bell market.

Now the four comes from the ratio of the captive to the independent markets in the United States but, in effect, it really is not as tough on Bell as it would be if the independents were the only other place they could go to sell competitively because they also have the whole rest of the world where they can go. Nevertheless, the ratio between the independent market and the captive market

in the United States is the ratio that generates the rather complicated provisions that are in the amendment.

The CHAIRMAN. Thank you.

Professor Baxter, according to recent newspaper accounts, the reports of the administration's task force stated that A.T. & T. had offered in prior settlement negotiations to divest certain portions of its equipment manufacturing operations. When questioned about this, the chairman of A.T. & T. reportedly denied that such an offer had ever been made. In light of these conflicting reports, would you please clarify for this committee what in fact was the substance of these prior negotiations?

Mr. BAXTER. I would like to say a couple of things preliminarily, if I may, Mr. Chairman.

First of all, I was not a party to any of those negotiations, so that my information is secondhand and hearsay. The second comment I would like to make is that I would ordinarily regard negotiations in any pending case as privileged with respect to my adversary. That is to say, I would feel I was double-crossing him to talk about negotiation discussions because if such discussions cannot occur in confidence, the process of attempting to settle cases would be made a great deal more difficult and more complex.

Notwithstanding that, it does seem to me that the chairman of the A.T. & T. Co. has to a limited extent waived that privilege in his own statements. However, I prefer to keep my statements at this time correspondingly narrow, and would not want to go into great detail about the discussions and settlement attempts that have occurred in the presently pending litigation. That says nothing about the prior cases.

I think the chairman of the company is correct in saying that in prior instances there had been no agreement on the part of A.T. & T. to spinoff any significant portion of Western Electric. In the pending case, in the negotiations that occurred before I arrived on the scene, there was tentative agreement. I do not know exactly how to put it because agreement was never, ever reached, and that is why there was no settlement, but there was a kind of tentative agreement in principle to a divestiture plan which would have called for spinning off some pretty good size pieces of Western Electric. Now, whether you call those significant or not, I do not know, so one would have to go back to the exact phraseology of his comment in order to know whether I was saying something that was entirely consistent or perhaps slightly inconsistent with his observation.

The CHAIRMAN. Professor Baxter, do you believe that if the court were to grant the divestiture remedy that the Justice Department is seeking in *United States* v. *American Telephone & Telegraph,* that this would result in lower consumer prices or greater diversity of service offerings to the consumer?

Mr. BAXTER. No one is entitled to sound 100 percent certain of his answer to that, Mr. Chairman. If I may, I am going to give you a longish answer to that question.

The situation in which we find ourselves is very complicated. I have no doubt there are substantial economies of vertical integration that are present in this industry, and they would be sacrificed

if one insisted on the kind of divestiture that we have been seeking in that case.

On the other hand, there is also a very substantial risk—and I believe reality—of cross-subsidization of the unregulated portions of the A.T. & T. Co. by the regulated portions. In one sense, divestiture is the only way that is certain to bring that cross-subsidization process to a halt. Furthermore, divestiture would bring that process to a halt without being accompanied by an extensive regulatory apparatus, so there is a trade-off between a clean solution to the cross-subsidization problem and sacrifice of the economies of vertical integration.

The legislation takes a rather different tack. It does not call for complete separation. It calls for the formation of so-called fully separate subsidiaries. That alone, of course, does not go very far toward solving the cross-subsidization problem but then it creates a regulatory body, for the most part the FCC, to police the line between the regulated components and the unregulated components.

One has to guess how successful the policing of that line will be. One has to guess the extent to which the fully separate affiliate device will itself, like divestiture, sacrifice some of the economies of vertical integration. Obviously, there is the drawback that it is a highly regulatory approach but no one can possibly claim to know exactly how those trade-offs will work out in an industry that is as dynamic, undergoing very, very rapid technological change, and is as complex as this industry is.

If one argues for divestiture, one argues that the cross-subsidy problem is terribly important, that the vertical integration economies probably are not very great, and that regulatory supervision is unwanted and more deregulation is possible. If one argues for the S. 898 approach, one says that the fully separate subsidiary device does not sacrifice significantly those economies of vertical integration, that the FCC will be able adequately to police that line, and therefore the cross-subsidy problem can be solved.

I think all I can tell you, Senator, is that I am content, enthusiastic even, about supporting S. 898 if it is amended to curb the two sources of cross-subsidy that we have previously talked about: the equal technical access at equal price for the competitive interexchange companies, and the equipment market problem that is addressed by the amendment, the open-market amendment we discussed previously.

The CHAIRMAN. Professor Baxter, what kind of a timetable would you realistically estimate for the final resolution of the lawsuit?

Mr. BAXTER. Well, that depends a good deal on what you think will happen. If we win the case—we can lose it rather more quickly——

[Laughter.]

Mr. BAXTER [continuing]. If we win the case, I would assume that the case will be submitted to the judge next spring, March, perhaps, with proposed findings, post-trial briefs. When, then, will the judge decide it? It is a case of enormous complexity with a large record but then we have an unusually able and determined judge who has done a magnificent job of running the case up until now. I would guess he would decide it in the spring of 1982, but that is a guess.

After he decides it, in all likelihood there will be an appeal to the Court of Appeals for the District of Columbia Circuit. The docket of the Court of Appeals for the District of Columbia is very, very crowded, and many cases that are appealed there wait around a long time. It would not be at all surprising if a year and a half passed before the court of appeals could address itself to the case and prepare an opinion. Again, the magnitude of the record and the complexity of the case bear on that.

Certainly, someone will apply for a writ of certiorari from the Supreme Court. Depending on what season of the year that occurs in, it might be heard at the next term of Court, or only in the next term after that. It is not at all unrealistic to imagine that that case might not yet have reached final judgment 5 years from now. Indeed, it would seem to me quite optimistic, if it goes the route I have described, to suppose that it may be resolved in less than 4 years, and one can readily imagine delays that would push the time horizon out to 6 or 7 years, although I think that that much delay is unlikely.

The CHAIRMAN. Professor Baxter, this administration has indicated it will actively enforce the antitrust laws, including seeking criminal sanctions where appropriate. How is this position consistent with the administration's decision to suspend and possibly eventually drop the suit against A.T. & T.?

Mr. BAXTER. A great deal more than the enforcement of the antitrust laws is involved in this situation. The telecommunications industry arguably is our most important industry even at the present time. The boundary lines between telecommunications and data processing and word processing are rapidly becoming blurred beyond recognition. I think there is almost no doubt that it will be our most important industry by a wide margin over the next quarter of a century.

The administration not only is entitled to have a telecommunications policy, it would be utterly irresponsible for the administration to fail to have a telecommunications policy. At the same time, the telecommunications industry at the present time consists predominantly of a single firm, the A.T. & T. Co.. One cannot talk about telecommunications policy without talking about the A.T. & T. Co.. It is the telecommunications industry in many senses.

An antitrust case is pending against the A.T. & T. Co. that involves all these same issues, with the consequence that one cannot talk about telecommunications policy without talking about that case. Therefore, it has been inevitable that the case has been drawn, implicitly and sometimes explicitly, into the entirely appropriate deliberations of the administration on these problems.

The matter is further complicated by the fact that the Attorney General and the Deputy Attorney General are recused, which has left me in the uncomfortable position of being the Attorney General de facto in all administration deliberations on these companies and at the same time being chief prosecutor in the A.T. & T. litigation. Again, complete separation of the two simply was and will continue to be impossible.

The administration reached a conviction that legislation was a superior solution, and that it was not possible to move legislation through the Congress while the case was there as a diversionary

factor. I pretend to be an antitrust lawyer, and pretend to be an economist, but I do not pretend to be a political seer. I have had, I do have, and I have expressed no opinion whatsoever on the extent to which that was a correct diagnosis of the situation in the Congress.

However, I do know that a lot of other people, rightly or wrongly, genuinely believed that and it was that belief on their part that led to the effort to put this case on ice, as I put it to the judge. I have never contemplated simply dismissing that case but it did not seem to me unreasonable—if these knowledgeable gentlemen were correct in their assessment—simply to put the case on hold for a period of time within which it was reasonable to contemplate that Congress might enact this legislation. Accordingly, I see no conflict whatsoever between the action we have taken in the A.T. & T. case and vigorous enforcement of the antitrust laws, to which I am very seriously committed.

The CHAIRMAN. Thank you.

Professor Baxter, I would like to ask you generally about the concept of a fully separated affiliate to conduct unregulated activities as proposed in S. 898. Quoting from the Department of Justice's reply comments in the FCC's communications systems CC docket No. 79-318 on page 16: "It is clear that the separate subsidiaries concept is likely to have a de minimis impact on moving incentives to the exercise of market power."

The FCC is also quoted in this document as stating that "If the parent has an incentive to exercise its market power to the disadvantage of consumers and competitors in the absence of a separate subsidiary, it has the same incentive to do so after one is required."

On page 17 of the reply comments it states: "The principle that separate entities operating under the same corporate umbrella are unlikely to prevent anticompetitive consequences has long been recognized by antitrust courts."

On page 18 it states:

> A separate subsidiary with separate offices, personnel, and books of account is unlikely to deter anticompetitive potentials. The officers and employees will still be part of the carrier's corporate umbrella, and thus subject to suggestion if not directives. Further, even if legions of accountants were used, it would be extremely difficult to determine whether cross-subsidization was actually occurring.

Do you agree with these statements regarding the general unacceptability of separate affiliates to protect competition?

Mr. BAXTER. In general I do agree with them. The first two statements, of course, address themselves only to incentives. Certainly creating fully separate subsidiaries does little if anything to change the incentives of the enterprise.

One simply must come to some individual belief about the efficacy of FCC administration of accounting systems for the purposes of achieving that objective. I must admit that I am skeptical of their ability to do so, and of course, it is that skepticism that has led me to urge market-oriented checks on the ability to engage in cross-subsidization.

Obviously, my sort of open-market amendment with respect to equipment is oriented in that frame of thinking. So, also, is the "equal access at equal prices" amendment to the interexchange problem. Therefore, I would say yes, for the reasons suggested in

the document from which you have been reading—which of course is a document that I am not sure I wrote all of but which crossed my desk at some point in time, and could hardly be expected to contain ideas that were unacceptable to me—S. 898 without amendments of the kind we have been discussing does not seem to me to be adequate.

The CHAIRMAN. You say S. 898 without the amendments——

Mr. BAXTER. That we have discussed earlier this morning——

The CHAIRMAN. That you have been discussing——

Mr. BAXTER. Would not seem to me to be acceptable.

The CHAIRMAN. Would not seem to be acceptable.

Professor Baxter, in light of the general problems with affiliates, would you say——

Mr. BAXTER. The general problems, Mr. Chairman, with what?

The CHAIRMAN. With affiliates.

Mr. BAXTER. Affiliates, yes, sir.

The CHAIRMAN. I have a southern accent. Excuse me. [Laughter.]

The CHAIRMAN. Would you say that the more stringent the separation requirement that exists between A.T. & T. and its fully separated affiliates—and after this we will call them FSA's for short—the more satisfactory this type of arrangement would be from an antitrust perspective?

Mr. BAXTER. I am reluctant to endorse that sweeping statement, Mr. Chairman. To me, antitrust enforcement is largely a matter of working for sound economic structures, and every time you heap another regulation on the boundary line between the FSA and the parent company, you impose additional costs, you sacrifice to a greater degree the economies of vertical integration to which I referred before, and I assume you gain something with respect to the cross-subsidization problem.

However, I think at every point one must keep in mind that one is engaging in tradeoffs between regulatory cost plus sacrifice of economies of vertical integration on the one hand, against tighter and tighter controls on the cross-subsidization problem. I am not sure that there is an answer in principle to how one optimizes that balance.

All I can say is that I think very careful policing of that boundary line is important; that the more one can resort to sensible prohibitions and objective, market-oriented tests, the better off one is. One has reduced the range of regulatory discretion, which I think is desirable. Nevertheless, one is going to wind up with a great deal of regulatory discretion, a large number of accountants, but I am not sure that every additional tightening of the screw is unambiguously a step in the right direction.

The CHAIRMAN. Professor Baxter, if the separations can be accomplished without regulations, would you generally agree that more separations result in greater safeguards?

Mr. BAXTER. If the separation can occur without regulation——

The CHAIRMAN. If the separations can be accomplished without regulations——

Mr. BAXTER. As by divestiture?

The CHAIRMAN. Would you generally agree that more separations result in greater safeguards?

Mr. BAXTER. Greater safeguards against cross-subsidization? I think unambiguously so.

The CHAIRMAN. Your answer is what?

Mr. BAXTER. Yes.

The CHAIRMAN. Yes?

Mr. BAXTER. Most certainly.

The CHAIRMAN. Thank you.

Mr. BAXTER. However, it comes with a cost.

The CHAIRMAN. Professor Baxter, let me ask you some questions regarding specific aspects of the separation provisions in S. 898. Under S. 898, the FSA—that is, the fully separate affiliate—is permitted to engage in joint ventures and partnerships with A.T. & T. Also, international activities are expressly exempted from all of the separation requirements otherwise applicable to the FSA. From an antitrust perspective, do you believe that these exemptions raise any problems in preventing or detecting cross-subsidization and other competitive abuses?

Mr. BAXTER. Yes, I do. Through any of those activities it is possible for a regulated enterprise to assume more than its fair share of the costs of a particular kind of activity, and thereby confer an economic benefit which can be used to engage in cross-subsidization on the other piece of the operation.

Whether the opportunity to engage in joint ventures, in partnerships, is sufficiently important to the preservation of economies of vertical integration to warrant that risk is a much more difficult question, and I do not at the moment have an answer to that question.

The CHAIRMAN. Professor Baxter, S. 898 expressly authorizes A.T. & T. management personnel to direct the operations of the FSA, and A.T. & T. is permitted to deal with the FSA in accordance with its independent, prudent business judgment. Do these provisions tend to undermine the separateness of these two operations on which this legislation is supposedly based?

Mr. BAXTER. Surely they do. Indeed, I would go further. So long as it is the case that the career objective of the man who is managing the local regulated telephone company is to wind up at 195 Broadway at some subsequent and happier time in his career, he will be enormously influenced in his behavior by the known preferences of A.T. & T. management. Furthermore, his salary will be determined by them. The amount of separateness that is achieved by the fully separate affiliate is very tenuous. That does not mean that it may not be the best solution.

The CHAIRMAN. Professor Baxter, S. 898 relies heavily on the ability of the FCC to allocate costs in order to assure that there is no cross-subsidization between the FSA and A.T. & T. This committee has heard a number of witnesses testify that the FCC is not capable of performing these activities, largely because they are virtually impossible to perform.

In any case, the FCC has been singularly unsuccessful in determining whether costs have been properly allocated in the past. From an antitrust perspective, do you believe the bill's heavy reliance on such cost allocation will be successful in preventing anticompetitive abuses?

Mr. BAXTER. It most certainly will not be successful in preventing any anticompetitive abuses. The problems of cost allocation are extremely difficult. I do not believe that A.T. & T. itself knows what its costs are, or indeed could know what its costs are with any great precision.

The FCC can try. It can do a very good job or a not very good job, but what a very good job consists of here is making some rough cuts, making some crude guesses. The extent to which common costs—costs which are common to two different kinds of activities—are present in this industry, first of all is large, and second of all is largely subject to the control of A.T. & T. They can design systems so that they have common costs to a greater degree than is necessary. Wherever the common cost problem is present, allocation of those costs to one activity or the other is theoretically impossible and is inescapably arbitrary in its implementation.

The CHAIRMAN. Professor Baxter, in light of the role of the FCC in this cost allocation, do you believe that the bill will result in its stated goal of deregulating the telecommunications industry?

Mr. BAXTER. Well, I take it its stated goal is not just the deregulation of the telecommunications industry. It will result in deregulation of customer premises equipment and of some service activities. It will impose some checks on the ability to cross-subsidize those activities from regulated activities. It will not deregulate major portions of the telecommunications industry, most certainly.

I really do not know how well it will succeed in achieving any one of those purposes, much less all of those purposes. Nevertheless, with the several amendments that we have previously discussed, I think it is a perfectly reasonable legislative attempt that is worthy of support in light of the present state of our information about this industry. I do not mean by saying that to suggest I would not be receptive to more amendments addressed to some of the problems that you have raised this morning.

The CHAIRMAN. Professor Baxter, although prohibited from jointly owning property, the FSA and A.T. & T. may jointly use property. Do you think that permitting this type of arrangement can lead to anticompetitive abuses which would be very difficult to identify in practice?

Mr. BAXTER. Yes. Again, it gives rise to a channel of possible cross-subsidization.

The CHAIRMAN. Professor Baxter, under S. 898 the FSA is permitted to own and operate transmission facilities and to offer transmission services which are the equivalent of services offered by the Bell operating companies in the longlines division. In a letter to Senator Schmitt, Mark Fowler, Chairman of the FCC, stated that this, and I quote, "could have the result of allowing A.T. & T. to transfer its market dominance to the unregulated sector without any determination as to the effect on users or competition." Do you agree with Mr. Fowler's statement?

Mr. BAXTER. I think Mr. Fowler's statement is an overstatement, provided that there is equal access at equal prices at the interconnection point. If it turns out to be economically desirable for interexchange carriers to build transmission facilities, why, the other interexchange carriers I assume will do so too. I see no reason to preclude a fully separate affiliate of A.T. & T. from having trans-

mission facilities. I think an adequate check is imposed on the risks as long as you take seriously the requirement of equal access to the local telephone company at the switch.

The CHAIRMAN. Counsel has a question right at this point she wishes to propound.

Mr. BAXTER. Yes, Mr. Chairman.

Ms. TIFFANY. Mr. Baxter, in S. 898, as currently drafted, the interconnection provisions only seem to apply to regulated carriers, not to the FSA's. Is the amendment that you are preparing on interconnection going to address interconnection with the FSA, which is unregulated, as well?

Mr. BAXTER. Well, it will address interconnection between the FSA and the regulated telephone company.

Ms. TIFFANY. Also other companies that would be interconnecting with the FSA?

Mr. BAXTER. Yes.

Ms. TIFFANY. Thank you.

The CHAIRMAN. Professor Baxter, in his minority views in the Commerce Committee report on S. 898, the distinguished junior Senator from South Carolina, Mr. Hollings, stated that there are:

> Substantial advantages to A.T. & T.'s offering of facilities in the separate affiliate on an unregulated basis. There are no interconnection requirements and the rates do not have to be just and reasonable. At the same time, A.T. & T. can maintain operating efficiencies since the parent and the separate affiliate can jointly plan and jointly use property.

This, he says:

> Would leave users at the mercy of the unregulated separate affiliate. Moreover, because the affiliate will be competing in offering transmission facilities, it is likely that A.T. & T. will focus its capital investments on research, development, and intervention on the unregulated market rather than on the basic public network which serves the smaller consumer.

Do you agree with these concerns regarding the anticompetitive potential of this provision in S. 898?

Mr. BAXTER. I am not really sure that I do. The only natural monopoly phenomenon, the only part of the telecommunications business where there cannot, as a practical matter be competition, is in the local exchange service. Indeed, even there that condition will continue only so long as it is necessary to run a strand of wire from the local telephone company to the customer's premises.

It does not stress our technological imagination to think of a day, 25 or 30 years from now, when it will be possible to have small parabolic antennas on everybody's roof and one can connect with any local telephone company one wants simply by retraining that antenna to a new laser pulse. However, until something of that kind comes along, the local telephone company is a natural monopoly and must, as a practical matter, be regulated.

However, with that exception I see no inescapable need for regulation and therefore no reason why we should not court vigorous competition in interexchange services, in the selling of telecommunications equipment, in the provision of data processing services, and in a wide variety of other activities. Mr. Hollings is really objecting to letting A.T. & T. participate in that competition, and I think it would be a great tragedy if a company as experienced, dy-

namic, and innovative as A.T. & T. has been were not permitted to participate in bare-knuckles competition in those areas.

The CHAIRMAN. I am going to allow Ms. Tiffany to proceed with questions. The next witness, Mr. Taft, we will take at about 2 o'clock.

Ms. TIFFANY. Mr. Baxter, with respect to customer premises equipment, S. 898 provides that although the FSA must eventually take over final assembly of such equipment and research and development activity for final assembly, it may nevertheless purchase subassembly components from A.T. & T., with the only restriction that A.T. & T. sell the same type of subassembly to nonaffiliates at the same charges and at the same terms and conditions.

As I understand it, a substantial amount of research and development goes into the subassembly manufacture, and indeed it is the subassembly that reflects the innovation of the manufacturer. Thus, it is unlikely that competitors who rely on innovation to sell their own in-customer-premise equipment will actually want to purchase A.T. & T. subassembly components for their own sale. If this is true, do you think this provision creates an opportunity for cross-subsidization from A.T. & T. to the FSA, which raises antitrust concerns?

Mr. BAXTER. Well, it does but, on the other hand, there is a fairly effective check on that because, since those subassemblies must be available at equal prices, the other companies have the opportunity to order large quantities of them. If they are being transferred to the FSA's below some reasonable measure of cost, the opportunity of other companies to get them at those same prices will impose very, very heavy costs on A.T. & T. That particular problem does not trouble me greatly.

Ms. TIFFANY. However, doesn't that assume that in fact other consumers will purchase those subassemblies rather than have their own?

Mr. BAXTER. If they are being offered below some reasonable measure of cost, I believe they will.

Ms. TIFFANY. And forego the innovation?

Mr. BAXTER. Yes, simply poach on Bell's innovation.

Ms. TIFFANY. Under S. 898, deregulation of certain of the FSA's activities will occur in 2 years, yet the structural separation that is supposed to substitute for regulation is not required to be completed for 6 years. Does this raise any concerns for you from an antitrust standpoint, and do you believe that such a lengthy transition period is really necessary?

Mr. BAXTER. I certainly believe a transition period is necessary, and the problems here are so serious that I guess I would accept almost any transition period in order to get to a sounder structure. I really do not know; 6 years seems like a long time to me.

Ms. TIFFANY. Do you think that the deregulation should be more equally paired up with the transition time?

Mr. BAXTER. No. I would like to see each piece of it to start moving as quickly as possible, and I do not think the 2-year provision on the finished assemblies is unreasonable. I really do not have a view on the reasonableness of 6 years for the structural changes. It seems long to me but I cannot rule out the possibility

that it may really be warranted. That is a technical question that I just do not feel able to address myself to very confidently.

Ms. TIFFANY. Section 214(g) of the bill seems to permit A.T. & T. to provide information about A.T. & T.'s network, such as operational protocols and technical interface requirements for connection with or use of regulated telecommunications services to the FSA before it is released to other competitors, and in some cases when it is not released at all. If this is a correct interpretation of the bill, would this raise anticompetitive concerns?

Mr. BAXTER. Yes, I think it would. I think, if that is a correct interpretation, I think it is a major defect in the bill.

Ms. TIFFANY. S. 898 permits virtually unlimited initial capitalization of the FSA by A.T. & T. and appears to place no limit on further capital contributions at a later time. While I understand that big is not necessarily bad, the FSA promises to be a truly giant operation, dwarfing most of its competitors which are dependent on outside financing and loans to provide their capital formation. Does this disparity create any competitive concerns for you?

Mr. BAXTER. I do not think so, not as long as the FSA is required to earn a rate of return on that capital that is as high as the rate of return being earned on the rest of the A.T. & T. Co., for example.

Ms. TIFFANY. Required by whom?

Mr. BAXTER. Well, by FCC implementation as to whether a failure to do that would really constitute a further capital contribution to the FSA by the parent company.

Ms. TIFFANY. This would be an FCC determination?

Mr. BAXTER. Yes.

Ms. TIFFANY. As you understand the bill, would this presently be required by the FCC of the FSA?

Mr. BAXTER. Well, they are required to approve subsequent capital transfers.

Ms. TIFFANY. Therefore, to the extent that the FSA would not be getting an adequate return on the investment, you would consider that a capital investment that the FCC would be overseeing?

Mr. BAXTER. That is the way I would read the bill. That certainly is not an inescapable reading of the bill, and perhaps it should be clarified.

Ms. TIFFANY. S. 898 permits A.T. & T. and the FSA to engage in joint institutional advertising to be allocated between them on a pro rata basis, however that may be determined. However, since it is competitive it seems that the FSA will probably benefit from this advertising more than will the monopoly regulated carrier. Isn't this another way cross-subsidization could occur between A.T. & T. and the FSA?

Mr. BAXTER. Yes. That is another example of the common costs about which I spoke earlier.

Ms. TIFFANY. S. 898 apparently permits employees to be transferred freely to and from the FSA and A.T. & T. In your opinion, does this raise the potential for anticompetitive abuses such as cross-subsidization by training FSA employees at A.T. & T. expense?

Mr. BAXTER. Yes, again that is quite right, simply by doing all your training at the parent company level and then transferring

them, and it also represents an avenue by which information can be conveyed without making it available to outside entities as the bill requires but will be very difficult to enforce.

Ms. TIFFANY. Under the 1956 consent decree, A.T. & T. was required to license its patents to nonaffiliates but under S. 898 there is no such requirement for the FSA. This would seem to allow A.T. & T. to transfer its patents to the FSA so as to avoid having to license them generally. Does this raise any anticompetitive concerns for you?

Mr. BAXTER. Well, again we read the bill differently. I would not read it to say that a patent obtained by the parent company and subsequently transferred to an FSA, as opposed to R. & D. done by the FSA which leads to a patent, was immune from the sharing obligation. Now if R. & D. is done by the FSA, and financed by the FSA out of its activities and leads to a patentable position, then I think it should be patentable and I do not think the FSA should be required to share it.

Ms. TIFFANY. Do you think that the special exemptions given to cable TV, newspaper publishers, and the alarm industry in S. 898 can be justified?

Mr. BAXTER. Only in political terms. [Laughter.]

Ms. TIFFANY. Does this indicate some lack of confidence in the separation provisions in S. 898 as adequate to prevent anticompetitive activity?

Mr. BAXTER. That certainly is a sensible interpretation. It is not the only interpretation, I suppose.

Ms. TIFFANY. Section 235(b)(2) of the bill directs the FCC to, within 2 years, determine what telecommunications services provided by regulated carriers at the time of enactment of the bill are and are not subject to effective competition, as that term is defined in section 203(c)(2) of the bill.

Section 203(c)(2), in turn, sets out a number of factors to be taken into consideration when making this determination. However, it is not at all clear that these factors would be the same that a court or the Justice Department would consider when determining relevant market power in the context of an antitrust proceeding. Do you believe there is any potential interference of the FCC's determination in these matters with a private litigant who brings an antitrust action in this area in which relevant market power would be a factor?

Mr. BAXTER. That is a very interesting question. I have never thought about that before. There is an explicit disclaimer of any antitrust immunity in the bill. Nevertheless, it would seem to me that any ruling the FCC had made in the context to which you refer certainly would be admissible in a rule-of-reason type inquiry in the judiciary, so that it might have a bearing and might tend to influence outcomes. It is not clear to me that that is undesirable. I am not sure now whether I have answered your question or not.

Ms. TIFFANY. Do you think that the bill could use some clarification on this point?

Mr. BAXTER. I do not have a present view on how I would like to see it clarified but it is always safe to answer a question by saying that further clarification would be possible.

Ms. TIFFANY. S. 898 proposes deregulation of WATS lines and private lines but not of MTS lines. Yet, according to testimony before this committee, WATS lines and MTS lines use virtually the same transmittal equipment and differ only in pricing mechanisms. Do you believe that there is any effective way of making certain that no cross-subsidies will flow from A.T. & T.'s MTS regulated services to its WATS unregulated services?

Mr. BAXTER. I do not think that poses any more difficult problem than a variety of other parts of the bill. I do not think that without divestiture you are ever really going to bring the cross-subsidization problem to the zero-risk level. However, as I have said before, there is a constant tradeoff and one cannot be sure that that is really the place you want to be in view of those tradeoffs.

Ms. TIFFANY. You do not think that there are any particular difficulties in trying to cost allocate in a situation where there are, in fact, the same transmission facilities being used for one service as opposed to another?

Mr. BAXTER. It is an area where one has a lot of common costs—and therefore serious problems of the kind I have previously identified—but the best solution, of course, would be more rapid deregulation of the MTS service.

Ms. TIFFANY. Do you have any opinion as to whether A.T. & T. has cross-subsidized its long distance rates with local loop revenues or vice versa?

Mr. BAXTER. Do you mean historically?

Ms. TIFFANY. Yes.

Mr. BAXTER. More vice versa.

Ms. TIFFANY. Therefore, you think that the local loop revenues——

Mr. BAXTER. No——

Ms. TIFFANY. Would you clarify what you——

Mr. BAXTER. Yes. Historically, A.T. & T. has subsidized local telephone service with longlines revenues.

Ms. TIFFANY. Do you believe that that is still occurring? Are you aware of any facts regarding that.

Mr. BAXTER. I think probably.

Ms. TIFFANY. Mr. Baxter, Mr. Cannon would like to ask you a question.

Mr. CANNON. Just one question, Mr. Baxter. In talking about the level of risk that cross-subsidization would occur, you said it is very difficult if not impossible to ever bring it down to the zero percent level. Do you have a fix in your mind as to what would constitute an acceptable level of risk? Have you thought about that?

Mr. BAXTER. I would find it very difficult to express it in quantifiable terms. I think one simply has to take each of these many, many phenomena that we have talked about and see how right one can make it—preferably using exterior market checks rather than discretionary regulatory checks whenever you can think of a way to do so—and take one's best intuitive guess as to the tradeoff with which you are left, between economies of vertical integration and the cross-subsidy risk.

Mr. CANNON. Is it something where you will know it when you see it, or——

Mr. BAXTER. I would carefully have avoided that phrase, but it is not an unfair way to put it.

Ms. TIFFANY. Mr. Baxter, we have talked about a number of various, particular areas in the bill that would lend themselves to anticompetitive abuses. Do you believe that amendatory language dealing with some or all of these areas would be appropriate?

Mr. BAXTER. Yes, I think so. Obviously, until I see it, and indeed others in the administration see it, one cannot promise support, but I certainly can promise receptivity.

Ms. TIFFANY. Most of these areas that we have discussed would not be addressed by the two amendments that the administration is currently considering.

Mr. BAXTER. That is correct.

Ms. TIFFANY. Do you believe that requiring some percentage of outside stockownership of the FSA would in any way decrease the potential of anticompetitive activity by A.T. & T. through that entity?

Mr. BAXTER. Not very much, unless it was a very large percentage.

Ms. TIFFANY. There was an amendment offered by Senator Hollings in the Commerce Committee markup that would require only 10 percent outside ownership, and the rationale was that this would provide both the public and the SEC as an additional watchdog in addition to the FCC. Do you think that this amendment has any validity?

Mr. BAXTER. Well, it certainly would have those effects. One is then left with the question whether three watchdogs are better than one, given that they all must be fed. [Laughter.]

Ms. TIFFANY. Have any studies been done or projections made by the Justice Department regarding the future developments that might be expected in the telecommunications industry over the next 10 years if S. 898 is enacted?

Mr. BAXTER. We did submit a paper that answers that general description, I guess, in the course of the documentary exchanges that were a part of the Cabinet Council consideration but, so far as I am aware, that is a confidential administration document that, so far as I know, has not been available.

Ms. TIFFANY. Are you free to discuss any of the conclusions reached in that document?

Mr. BAXTER. I have already expressed as my presently held state of mind some things that were also stated in that document, and I would prefer to stay on that plane and not purport to talk about what is in that document. I am not at liberty to attribute anything to that document, still less to produce it.

Ms. TIFFANY. Mr. Baxter, I understand that your special expertise is in antitrust. However, I wonder if you would care to comment on whether you believe there are any constitutional problems that might arise as a result of S. 898's express modification of the 1956 consent decree, while at the same time expressly not modifying the underlying antitrust laws on which the decree was based?

Mr. BAXTER. Well, I am not a constitutional lawyer, and discretion would undoubtedly lead me to decline your invitation, but it seems to me even an amateur constitutional lawyer could conclude

with a fair amount of confidence that there is no serious constitutional problem.

Ms. TIFFANY. Thank you. I believe that Mr. Cannon has a few more questions to ask you, Mr. Baxter.

Mr. CANNON. I said, I believe it was reported in March of this year that Secretary Weinberger, the Secretary of Defense, had expressed some concerns about the continuation of the suit, and in fact expressed some desire that the suit should be dropped. Did you have any occasion or chance to speak with the Secretary or any of his staff about his comments?

Mr. BAXTER. Yes. Shortly after I learned of that, I called Secretary Weinberger's deputy and asked that we be more fully informed just what those concerns were. Subsequently, representatives were sent over from the Defense Department and we talked about the problem. They said they would get us an articulation of their concerns; indeed, we hoped to have it in time to embody it in the lawsuit, but it proved more time-consuming than they expected, and we did not in fact receive anything from the Department until after we had finished putting in our evidence.

Then ultimately, some time early in July, we did receive a thick document stating their concerns. That, too, was a Cabinet Council document which, so far as I know, is supposed still to be confidential. We prepared a response to that which has again the same character, so there has been some exchange with the Defense Department on that topic.

Mr. CANNON. Were you not notified in advance that Secretary Weinberger was going to make the statements he made about dropping the case?

Mr. BAXTER. No; I was not.

Mr. CANNON. Who was the deputy that you talked to when you called?

Mr. BAXTER. Mr. Carlucci.

Mr. CANNON. Who were the representatives that came to the Department to discuss this matter?

Mr. BAXTER. Well, the first—I cannot reproduce all the names, although I would be happy to send them to you—the first delegation was led by Mr. Nederlander, who has been around the Defense Department for quite a long time. Subsequent delegations were led by Will Taft, who is, I think, right over my left shoulder.

Mr. CANNON. I believe you said they were going to express or did express their concerns with the suit. Are you at liberty to discuss some of those concerns at this point?

Mr. BAXTER. No, because I would be quoting from a document which, so far as I am aware, is still supposed to be confidential, although I gather there is some doubt about that. I would prefer not to do that.

Mr. CANNON. Was there a discussion between you and your staff, or among members of your staff, about how the Defense Department's concerns would be embodied in the lawsuit or in the Department's presentation of evidence?

Mr. BAXTER. To some extent there was; yes. We had rather hoped that we could have a Defense Department witness go on during the course of our case and say, "Well, divestiture at this point in the switch would not be troublesome to us but divestiture at that point

would be," or something of the sort, but that did not prove to be possible.

Mr. CANNON. How far advanced was this strategy in terms of selecting a person to testify, selection of expert witnesses, or that sort of thing?

Mr. BAXTER. It did not get very far. The Defense Department first expressed a hope to have a document to us about June 1—this all got started only mid-spring—which would have given us a couple of weeks to get a witness ready. It would be a short time even at that but in fact we did not receive the document until 2 or 3 days after our part of the case had closed.

Mr. CANNON. Did you notify the Department that, for instance, your part of the case was closing, and that if they wanted to present a witness it would have to be done quickly?

Mr. BAXTER. The schedule was well-known when we met. I am sure we talked about those dates. I could not be absolutely positive. I do not think there was a mystery about that. We went back around the first of June and said, "Can we hope to see it soon?" Someone said—and I am not even sure who now—"Well, now we think we will have it ready by June 15," but in fact we did not get it until early July.

Mr. CANNON. What was the purpose of receiving the document after the Government had closed its case?

Mr. BAXTER. Well, of course by that time the whole Cabinet Council consideration of this problem was in full swing, so that the document that I am referring to as the one that we eventually got was the one that came through the Cabinet Council process and to which we responded in the Cabinet Council process, but I treated that as a response also pursuant to our earlier discussions because, at least in part, it addressed the same questions.

Mr. CANNON. Did the Department of Defense document—and we will ask Mr. Taft this later on, I am sure, as well—address the specific problems of divestiture as set forth in the Government's case?

Mr. BAXTER. I would rather let Mr. Taft talk to that.

Mr. CANNON. How about the document that the Department of Justice prepared in response to the Defense Department?

Mr. BAXTER. Yes, it did talk but not at a level of great technicality. It is a plain language document for the most part.

Mr. CANNON. Since that time, have there been any other discussions between your office and the Defense Department about the ongoing case, or any decision to continue the case or dismiss the case?

Mr. BAXTER. Not any of which I am aware.

Ms. TIFFANY. Mr. Baxter, I believe that is all the questions we have for you. We thank you very much for appearing at this rather lengthy hearing.

Mr. BAXTER. Thank you.

Ms. TIFFANY. The hearing will be in recess until 2 o'clock this afternoon.

[Whereupon, at 12:52 p.m., the committee recessed, to reconvene at 2 p.m. the same day.]

AFTERNOON SESSION

The CHAIRMAN. The committee will come to order.

Mr. Taft, if you will come around and hold up your hand to be sworn. Do you swear that the evidence you give in this hearing shall be the truth, the whole truth, and nothing but the truth, so help you God?

Mr. TAFT. I do.

The CHAIRMAN. You may proceed.

TESTIMONY OF WILLIAM H. TAFT IV, GENERAL COUNSEL, U.S. DEPARTMENT OF DEFENSE

Mr. TAFT. Thank you, Mr. Chairman.

I am pleased to appear in response to your request to discuss the Department of Defense's involvement in the ongoing Government antitrust suit against the American Telephone & Telegraph Co. I have a very short statement if you would like me to read it, or I will submit it for the record, whichever you would prefer.

The CHAIRMAN. I believe we invited Secretary Weinberger, but I understood President Sadat is here and that he had some emergency situations, so he has asked you to appear in his place. Is that correct?

Mr. TAFT. That is correct, sir. I did not mean to imply that your invitation had been extended to me personally.

The CHAIRMAN. No; I just wanted to explain for the record, that we did invite the Secretary of Defense and that you are representing him.

Mr. TAFT. Yes, sir.

The CHAIRMAN. All right. You may proceed.

Mr. TAFT. I understand that you have called these hearings to consider the background of the recent request by the Justice Department for a continuance of that lawsuit. That request was, of course, denied by the court.

The Department of Defense, and indeed the entire Government, are large users of telecommunications services. Telecommunications facilities which support the needs of the Federal Government are generally under the ownership and operational control of privately owned, regulated companies.

The Government obtains over 85 percent of its total needs and more than 94 percent of its most critical circuits from those privately owned companies. Governmental actions regarding military forces, national mobilization, continuity of Government, and many other vital governmental missions, are executed through the use of telecommunications facilities provided by commercial companies.

In fulfilling our mission of national security and emergency preparedness, the Department of Defense requires a telecommunications system that is survivable, restorable, and credible, that is seen to be so. These attributes are necessary to help our Nation survive natural disasters and emergencies, which may of course be either civilian or military in nature.

The Department of Defense has undertaken an analysis of the effects of a court order requiring A.T. & T. divestiture of its manufacturing, research, and longlines components from the local operating companies upon national defense and security, and emergen-

cy preparedness. In the preparation of its analysis, the Defense Communications Agency has met with representatives of Government and of industry.

In addition, I and members of my staff, as well as technical experts from the Department, have met with representatives of the Justice Department to discuss the relief options being contemplated by the Department in the A.T. & T. suit. The conclusion reached by our analysis is that court-ordered divestiture could cause substantial harm to our national defense and security, and emergency preparedness telecommunications capabilities.

Specifically, we concluded, one, from a national defense and security and emergency preparedness standpoint, the telecommunications network cannot properly be artificially divided between intercity and local exchange functions. The network necessary to meet our critical communications needs is the present integrated, phone instrument to phone instrument capability.

Two, today that telecommunications network is extensively and intensively designed, planned, constructed, operated and managed by American Telephone & Telegraph, with the cooperative participation of the independent telephone companies.

Three, this network planning and management process involves extensive interaction among all entities of the Bell System, and requires customer-premises to customer-premises technical, operational, and economic planning.

Four, currently only the Bell System, with the cooperative participation of the independent companies, has the incentive or the ability to conduct the necessary network planning and management.

Five, artificial division of the Bell System between local exchange and intercity functions ignores the physical and functional operation of the telecommunications network, will reduce or eliminate the incentives for the Bell operating companies to participate in joint network planning and management, and will eventually result in fragmentation of the nationwide telecommunications network.

In our view, the restructuring of the telecommunications industry is of great importance. As a major customer, the Department looks forward to enjoying the benefits that all customers will receive from deregulation.

At the same time, however, the needs of national security must be recognized and provided for in any restructuring. The Congress should establish the fundamental goals of, and guidelines for, national communications policy in the eighties and beyond with these considerations in mind. This approach can, we believe, be effectively pursued through enactment of S. 898, if it is amended as the administration has proposed and as further described by Mr. Baxter this morning.

I appreciate the opportunity to testify and I will be glad to try and answer your questions, sir.

The CHAIRMAN. Thank you, Mr. Taft. I have a few questions here I would like to propound to you.

Are you the General Counsel for the Defense Department?

Mr. TAFT. Yes, sir, I am.

The CHAIRMAN. Incidentally, I believe you are a grandson of former Senator Robert Taft, aren't you, and a great-grandson of President Howard Taft?

Mr. TAFT. That is right.

The CHAIRMAN. Mr. Taft, I would like to begin my questions with you at the point we left off with Professor Baxter. When Secretary Weinberger announced in March that he believed the A.T. & T. suit should be dropped, do you know if he had consulted with any administration officials outside the Defense Department about that statement?

Mr. TAFT. I do not believe that he had at that time. I believe that the statement that he made was made, in fact, to the Armed Services Committee of the Senate in response to a question that was put to him.

The CHAIRMAN. Prior to Secretary Weinberger making that statement, was there any question raised as to whether the Justice Department should be notified about the statement?

Mr. TAFT. No, sir. I think the circumstances in which the statement was made precluded that.

The CHAIRMAN. Mr. Taft, do you know the reason why the Defense Department was unable to coordinate with the Justice Department in time for a Defense Department witness to be presented on behalf of the Government during the A.T. & T. trial?

Mr. TAFT. I do not know of any reason why that could not have happened. I do not believe that there was a real desire on the part of the Government to do this, or a feeling that it was necessary to an effective presentation of the case. We did not receive any strong indication from the Justice Department that this was a necessary part of their case, and we did not feel that we should push them to put somebody on it. I do not think that it was an issue that arose very strongly from their side.

The CHAIRMAN. Mr. Taft, did you participate in the task force working group?

Mr. TAFT. Yes, sir, I did.

The CHAIRMAN. You did participate?

Mr. TAFT. I did.

The CHAIRMAN. Mr. Taft, do you recall any discussion as to whether the Justice Department should be included in the task force?

Mr. TAFT. No. When I was first informed of the task force's existence, they were not included and the only discussion I would remember was, I mentioned that I noticed that they were not included, and the reasons that Secretary Baldrige gave this morning essentially were given to me at that time.

The CHAIRMAN. Mr. Taft, you were a member of the task force, I believe you said.

Mr. TAFT. Yes; I was.

The CHAIRMAN. What specific work did you do on the task force?

Mr. TAFT. I worked with Mr. Unger and Mr. Lawrence and the other members reviewing the papers that had been prepared by the Commerce Department staff. I worked with the people in the Defense Communications Agency and my own office reviewing those and getting comments back to the Commerce Department, which of course was chairing the working group. We exchanged further

drafts and then I attended the meeting of the task force to finally agree on the final draft of the work group.

The CHAIRMAN. Mr. Taft, do you personally feel the A.T. & T. case has been affected by the work of the task force and the Cabinet Council?

Mr. TAFT. I feel that to the extent that the result of the task force's work went into the Cabinet Council, and then as a result of deliberations there Attorney General Baxter went to the court and asked for a continuance, that would have been an outgrowth of the work that we did. However, beyond that, I think that the request for the continuance, in terms of the actual presentation of the case, did not have an effect on it.

The CHAIRMAN. Mr. Taft, do you recall how soon after the task force was formed that the first draft of the task force report was written?

Mr. TAFT. That would have been in mid-June some time. It was 2 or 3 weeks after the forming of the task force, as I recall.

The CHAIRMAN. Mr. Taft, did you consult with anyone at the Justice Department during the drafting of the task force report?

Mr. TAFT. Not about the task force report. We were, of course, in touch with the Justice Department separately about the lawsuit.

The CHAIRMAN. Mr. Taft, is it a fair statement that the work of the task force affected the A.T. & T. case regardless of the merits of the case?

Mr. TAFT. I think only to the extent that I have indicated, that it did result in the request for a continuance being made.

The CHAIRMAN. Counsel will propound some questions.

Mr. CANNON. Mr. Taft, let me ask you about Presidential Directive No. 53 issued by President Carter on November 15, 1979. As you know, the subject of this directive is "National Security Telecommunications Policy."

In this directive, the President stated that it is essential to the security of the United States to have telecommunications facilities adequate to satisfy the needs of the Nation during and after any national emergencies. The President then went on to outline telecommunications policy principles and, of course, the objectives a policy would hope to accomplish.

We have yet to find anyone who says this directive does not correctly state the need for a security telecommunications policy. Are you basically in agreement with Presidential Directive No. 53?

Mr. TAFT. Yes; I think we are. We are carrying it out. Of course, all of the Presidential directives from the prior administration are being reviewed, but that one I think is one that we are certainly pursuing and carrying out.

Mr. CANNON. OK. As we have said, there is general agreement that something must be done to foster and promote a more unified, coordinated security telecommunications policy. The question must now be, How do we best go about it and what do we expect to achieve?

We have a copy of the June 11, 1981, testimony of Lt. Gen. William Hilsman, who as you know is Director of the Defense Communications Agency, before the Senate Commerce Committee. I believe that your testimony to a certain degree echoes General Hilsman's testimony, that his agency requires that a communications

policy have three basic attributes, which are survivability, restorability, and credibility.

First let me ask you, do you agree that these are the appropriate goals an effective system should strive to meet?

Mr. TAFT. Yes, indeed.

Mr. CANNON. I want to move to several reports that have been written that I am sure you are familiar with, and ask you to comment on those. First there is a February 1981 report which was prepared by the Stanford Research Institute. It is entitled "A Review of National Security Emergency Preparedness Telecommunications Policy." This report was prepared for the National Communications system in Washington. Are you familiar with that report?

Mr. TAFT. Yes; I have seen two reports from the Stanford group, and I am not sure of the dates of each one of them but I think one of them was that date.

Mr. CANNON. Then were was another SRI report, as you mentioned, dated January 1981 which is entitled "A Brief Analysis of National Security and Emergency Preparedness Implications," concerning relief contentions in the Justice Department's civil action 74-1698. This report, we understand, was prepared for A.T. & T. Longlines. Are you familiar with that report?

Mr. TAFT. Yes; that would be the second report that I saw.

Mr. CANNON. It would appear that the SRI report prepared for the National Communications system is most sharply critical of the lack of Government coordination of a defense and emergency telecommunications system. In fact, the report notes that:

> Although telecommunications capabilities are critically important in the pursuit of peace through strength, one would not be able to discern this importance of telecommunications in national security and emergency preparedness from the haphazard and feeble attention often afforded to these critical factors in the telecommunications forums of the Federal Government.

The report further notes that the net result of this fragmentation is frustration and uncertainty as to the direction and management of telecommunications initiatives in the event of disaster. If you could follow that, do you agree with these statements?

Mr. TAFT. I do not want to underestimate at all the importance and largeness of the task that we have in keeping our communications system intact and in strengthening it at every opportunity that we have. I think that it has today some strong aspects and things that we can be proud of. Obviously there are many improvements that we can make and we hope to make.

Mr. CANNON. Now the reports seem to say different things. The SRI report for the A.T. & T. Longlines appears to echo the sentiment of Secretary Weinberger in March, and it predicts that great harm to our defense and emergency communications system could occur if the Bell System is split in any significant way.

On the other hand, the SRI National Communications System report sets forth the vulnerability of our present system. That report notes that centralization of functions is a poor practice if communications are to be available during major emergency or crisis situations. The loss of just 20 facilities, the report notes, destroys the entire long-distance telephone system in the United States.

All in all, the report concluded that the A.T. & T. system appears to be vulnerable to large-scale nuclear attacks, direct terrorist attack, and to widespread national disaster. Therefore, it appears that on the one hand one report says that we need to keep the present system intact, and the other report says that keeping the system intact appears to make the telecommunications system more vulnerable. I guess the question here is very simple; that is, which of these two reports do you think is correct, or can they be reconciled?

Mr. TAFT. I think that in terms of the vulnerabilities of the system that were identified—and I do not necessarily subscribe to all of the ones that were identified in that report—but that the best system we have, let us say, may have some vulnerabilities, is not a reason to abandon it, because it is the best system we have. We should keep it; we should work to get rid of the vulnerabilities. We should introduce additional systems, if that is what is necessary, but I do not see that the best system we have has some vulnerabilities is a reason to call it anything other than the best system we have.

Mr. CANNON. Getting back to the three characteristics of a communications policy—survivability, restorability, and credibility—I believe that both you and General Hilsman have testified that restorability essentially means alternate routing, facilities redundancy, an interconnection and interoperation capability sufficient to provide rapid restoration of service to damaged areas of the Nation. Of course, survivability means a system that is able to effectively perform during and after a disaster or a period of military conflict.

Now do you believe that these two characteristics, restorability and credibility, can effectively be created or effectively be reached with the present system as it is, without divestiture?

Mr. TAFT. I do not believe that divestiture will assist in reaching them. There are, as I mentioned and as General Hilsman has identified more elaborately in his testimony, things that we would like to do to strengthen the system, in point of view of its survivability and in point of view of its restorability. I think that we should work with what we have and improve it.

Mr. CANNON. Mr. Taft, are you of the opinion now that divestiture will amount to essentially getting rid of the present system as it now stands?

Mr. TAFT. It would depend on what sort of divestiture it was and what the terms and conditions for the relationships between divested companies might be. All sorts of different scenarios are possible. There are circumstances of divestiture that cause us considerable concern.

Mr. CANNON. We were wondering. I mean, isn't it true that within the United States we have a number of independent telephone companies that essentially are not part of the one system, and that these independent phone companies interconnect without widespread continuity or interconnection problems in this entire system?

Mr. TAFT. That is correct. They do, however, have at the center of that system—and I think Attorney General Baxter made this point, also, this morning—a very large single entity. What may

work well when it is interconnecting with a large single entity may not work so well when it is just a lot of smaller entities.

Mr. CANNON. Counsel has one question.

Ms. TIFFANY. Mr. Taft, the divestiture that the Justice Department is seeking in the lawsuit, as I understand it, is to separate the Bell operating companies from the Longline Division. Again, there are a number of independent operating companies that interconnect with the Bell Longline Division, and so you do have that central heart of a system that interconnects different companies in different parts of the country. Do you envision that the divestiture that would be sought by the Justice Department, separating out the other Bell operating companies, would result in the loss of that system?

Mr. TAFT. We do not know what would happen to the operating companies that were separated from the longlines, whether they would stay together or whether they would separate. There have been different proposals. We also do not know, of course, what the court might do with any suggestion that was made by the Justice Department, whether it would accept it or perhaps adopt a remedy of its own choosing.

The remedy that is proposed by the Justice Department, insofar as I understand it, would only divide A.T. & T. into two companies: The operating companies, which would be locally regulated, would remain as one company with its 20 or however many subsidiaries there are in it; and then the longlines, Western Electric, Bell Labs, and the general divisions would be another company. In the absence of any legislation—that would result, we feel, in a lessening of the ability for planning and managing the single system which we rely on now, which is extremely beneficial to us, and which we require.

Ms. TIFFANY. Do you find that management and planning suffer because of the longlines interconnections with a lot of independent companies?

Mr. TAFT. No, we do not today find that, but the interconnections with those companies are a small portion of the total interconnections. We find that the central system has an incentive to plan and an incentive to respond as a single system to us now, in the requests and demands that we put on it.

We do not know that that would continue if there were not such a central system. The central system has incentives to respond and to plan in a coordinated manner that a fragmented system would not, or that the individual components of a fragmented system would not.

Ms. TIFFANY. Mr. Taft, do you know what portion of the system depends on independent telephone companies and interconnections?

Mr. TAFT. I believe it is about 20 percent at the local operating level; 80/20 is what we have been using here today.

Mr. CANNON. Mr. Taft, let me ask you one question about the prior testimony of General Hilsman and Dr. DeLaver before the Commerce Committee. In their testimony, they both note that the Defense Department would be submitting suggested amendments to S. 898.

Specifically, we note that General Hilsman stated that S. 898 should contain a provision authorizing and insuring that all telecommunications carriers develop and participate in joint carrier planning and centralized network management. Do you know if there was ever an amendment submitted to the committee to that effect?

Mr. TAFT. I believe there was, and I believe it was included in the bill as reported.

Mr. CANNON. Do you know what section that was in?

Mr. TAFT. Well, let me see. I do not have a section number. I gather it was section 238.

Mr. CANNON. To your knowledge, that was specifically a Defense Department amendment?

Mr. TAFT. It was drafted by us, and we were delighted that it was included in the bill.

Mr. CANNON. Did you coordinate this through the Commerce Department, that is, the submitting of amendments to the legislation?

Mr. TAFT. Yes, indeed we did. It was coordinated through the entire administration and accepted by the administration.

Mr. CANNON. Are you aware of other amendments from other parts of the administration that were submitted to the Commerce Committee and that eventually found their way into the bill?

Mr. TAFT. Well, we submitted some additional amendments to the purposes clause that would have put national defense as one of the purposes that should be considered, and a variety of other minor, less important amendments, but not so minor that we did not feel that they should be included.

I believe the Commerce Department itself had a considerable number of amendments to S. 898—this is as it was originally introduced—most of which were incorporated by the committee. Then, of course, the Justice Department had two, at least two amendments which we support, which were not included but which we are extremely hopeful will be included on the floor.

Ms. TIFFANY. Mr. Taft, does A.T. & T. perform any services for the Department of Defense free of charge?

Mr. TAFT. I do not believe so.

Ms. TIFFANY. Aren't there some services, planning services and other organizational services, that are provided to the Department of Defense by A.T. & T. and not specifically charged for?

Mr. TAFT. Well, I am not aware of any. I guess I would like to check with the people who get billed and do not get billed for these things. We are charged an awful lot by them, and it seems to me it ought to cover whatever they do for us.

Ms. TIFFANY. If you would check on that and submit an answer for the record, we would appreciate it.

Mr. TAFT. Yes.

[The following was subsequently supplied for the record:]

AT&T does not perform any services for the Department of Defense free of charge. As a regulated enterprise, AT&T recovers all of its expenses and investment, including a return on the latter, through its tariffed rates filed with the Federal Communications Commission and state regulatory bodies. Pursuant to those tariffs the Department of Defense annually pays to Bell System Companies nearly $200 million for long-haul telecommunications and approximately $360 million for other telecommunications services.

The CHAIRMAN. Mr. Taft, I believe that is about all the questions we have for you today. I want to thank you for your appearance here, and express our regards to Secretary Weinberger, and tell him that we will not call him unless we feel the need to do so, since you have come today to represent him. If we do feel the need later, we will get in touch with him.

Mr. TAFT. He will be delighted to come, I am sure.

The CHAIRMAN. Thank you very much.

The committee stands adjourned.

[Whereupon, at 3:23 p.m., the committee recessed, to reconvene at the call of the Chair.]

[Prepared statement of Hon. William H. Taft IV follows:]

STATEMENT OF HONORABLE WILLIAM H. TAFT, IV
GENERAL COUNSEL OF THE DEPARTMENT OF DEFENSE

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

I AM PLEASED TO APPEAR IN RESPONSE TO YOUR REQUEST TO DISCUSS THE DEPARTMENT OF DEFENSE'S INVOLVEMENT IN THE ONGOING GOVERNMENT ANTITRUST SUIT AGAINST THE AMERICAN TELEPHONE AND TELEGRAPH COMPANY. I UNDERSTAND THAT YOU CALLED THESE HEARINGS TO CONSIDER THE BACKGROUND OF THE RECENT REQUEST BY THE JUSTICE DEPARTMENT FOR A CONTINUANCE OF THAT LAW SUIT. THE REQUEST WAS, OF COURSE, DENIED BY THE COURT.

THE DEPARTMENT OF DEFENSE AND, INDEED, THE ENTIRE GOVERNMENT ARE LARGE USERS OF TELECOMMUNICATIONS SERVICES. THE TELECOMMUNICATIONS FACILITIES WHICH SUPPORT THE NEEDS OF THE FEDERAL GOVERNMENT ARE GENERALLY UNDER THE OWNERSHIP AND OPERATIONAL CONTROL OF PRIVATELY OWNED REGULATED COMPANIES. THE FEDERAL GOVERNMENT OBTAINS OVER 85% OF ITS TOTAL NEEDS AND MORE THAN 94% OF ITS MOST CRITICAL CIRCUITS FROM THESE PRIVATELY-OWNED COMPANIES. GOVERNMENTAL ACTIONS REGARDING MILITARY FORCES, NATIONAL MOBILIZATION, CONTINUITY OF GOVERNMENT AND MANY OTHER VITAL GOVERNMENTAL MISSIONS ARE EXECUTED THROUGH THE USE OF THE TELECOMMUNICATIONS FACILITIES PROVIDED BY COMMERCIAL COMPANIES.

IN FULFILLING OUR MISSION OF NATIONAL SECURITY AND EMERGENCY PREPAREDNESS, THE DEPARTMENT OF DEFENSE REQUIRES A TELECOMMUNICATIONS SYSTEM THAT IS SURVIVABLE, RESTORABLE, AND CREDIBLE. THESE ATTRIBUTES ARE NECESSARY TO HELP OUR

NATION SURVIVE NATURAL DISASTERS AND EMERGENCIES, WHICH MAY BE CIVILIAN OR MILITARY IN NATURE.

THE DEPARTMENT OF DEFENSE HAS UNDERTAKEN AN ANALYSIS OF THE EFFECTS OF A COURT ORDER REQUIRING AT&T DIVESTITURE OF ITS MANUFACTURING, RESEARCH AND LONG-LINES COMPONENTS FROM THE LOCAL OPERATING COMPANIES UPON NATIONAL DEFENSE AND SECURITY, AND EMERGENCY PREPAREDNESS. IN THE PREPARATION OF ITS ANALYSIS THE DEFENSE COMMUNICATIONS AGENCY HAS MET WITH REPRESENTATIVES OF GOVERNMENT AND INDUSTRY. IN ADDITION, I AND MEMBERS OF MY STAFF, AS WELL AS TECHNICAL EXPERTS FROM THE DEPARTMENT HAVE MET WITH REPRESENTATIVES OF THE JUSTICE DEPARTMENT TO DISCUSS THE RELIEF OPTIONS BEING CONTEMPLATED BY THE JUSTICE DEPARTMENT IN THE SUIT. THE CONCLUSION REACHED BY OUR ANALYSIS IS THAT COURT-ORDERED DIVESTITURE COULD CAUSE SUBSTANTIAL HARM TO OUR NATIONAL DEFENSE AND SECURITY, AND EMERGENCY PREPAREDNESS TELECOMMUNICATIONS CAPABILITIES. SPECIFICALLY WE CONCLUDED:

1. FROM A NATIONAL DEFENSE AND SECURITY AND EMERGENCY PREPAREDNESS STANDPOINT, THE TELECOMMUNICATIONS NETWORK CANNOT PROPERLY BE ARTIFICALLY DIVIDED BETWEEN INTERCITY AND LOCAL EXCHANGE FUNCTIONS. THE NETWORK NECESSARY TO MEET OUR CRITICAL COMMUNICATIONS NEEDS IS THE PRESENT INTEGRATED "PHONE-INSTRUMENT TO PHONE-INSTRUMENT" CAPABILITY.

2. TODAY, THAT TELECOMMUNICATIONS NETWORK IS EXTENSIVELY AND INTENSIVELY DESIGNED, PLANNED, CONSTRUCTED, OPERATED AND MANAGED BY AMERICAN TELEPHONE AND TELEGRAPH, WITH THE COOPERATIVE PARTICIPATION OF THE INDEPENDENT TELEPHONE COMPANIES.

3. THIS NETWORK PLANNING AND MANAGEMENT PROCESS INVOLVES EXTENSIVE INTERACTION AMONG ALL ENTITIES OF THE BELL SYSTEM AND REQUIRES CUSTOMER-PREMISES TO CUSTOMER-PREMISES TECHNICAL, OPERATIONAL AND ECONOMIC PLANNING.

4. CURRENTLY, ONLY THE BELL SYSTEM, WITH THE COOPERATIVE PARTICIPATION OF THE INDEPENDENTS, HAS THE INCENTIVE OR THE ABILITY TO CONDUCT THE NECESSARY NETWORK PLANNING AND MANAGEMENT.

5. ARTIFICIAL DIVISION OF THE BELL SYSTEM BETWEEN LOCAL EXCHANGE AND INTERCITY FUNCTIONS IGNORES THE PHYSICAL AND FUNCTIONAL OPERATION OF THE TELECOMMUNICATIONS NETWORK, WILL REDUCE OR ELIMINATE THE INCENTIVES FOR THE BELL OPERATING COMPANIES TO PARTICIPATE IN JOINT NETWORK PLANNING AND MANAGEMENT, AND WILL EVENTUALLY RESULT IN FRAGMENTATION OF THE NATIONWIDE TELECOMMUNICATIONS NETWORK.

IN OUR VIEW, THE RESTRUCTURING OF THE TELECOMMUNICATIONS INDUSTRY IS OF GREAT IMPORTANCE. AS A MAJOR CUSTOMER, THE DEPARTMENT LOOKS FORWARD TO THE BENEFITS THAT ALL CUSTOMERS WILL RECEIVE FROM DEREGULATION. AT THE SAME TIME, HOWEVER, THE NEEDS OF NATIONAL SECURITY MUST BE RECOGNIZED AND PROVIDED FOR IN ANY RESTRUCTURING. THE CONGRESS SHOULD ESTABLISH THE FUNDAMENTAL GOALS OF AND GUIDELINES FOR NATIONAL COMMUNICATIONS POLICY IN THE 1980S AND BEYOND WITH THESE CONSIDERATIONS IN MIND. THIS APPROACH CAN, WE BELIEVE, BE EFFECTIVELY PURSUED THROUGH ENACTMENT OF S.898 IF IT IS AMENDED AS THE ADMINISTRATION HAS PROPOSED.

I APPRECIATE THE OPPORTUNITY TO TESTIFY THIS MORNING.

DOJ OVERSIGHT: *U.S.* v. *AT&T*

MONDAY, JANUARY 25, 1982

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The committee met, pursuant to notice, at 9:30 a.m., in room 1202, Dirksen Senate Office Building, Senator Strom Thurmond (chairman of the committee) presiding.

Present: Senators Thurmond, Hatch, Specter, and Metzenbaum.

Staff present: Steve Cannon, chief counsel for antitrust; Marcy Tiffany, counsel for antitrust and chief economist; Peter Chumbris, senior counsel for antitrust; Mary Louise Westmoreland, counsel; John Nash, counsel; Bruce Cohen, counsel; and Margery Baker, minority chief counsel.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The CHAIRMAN. The committee will come to order.

Two weeks ago, the Justice Department brought to conclusion two of the most significant antitrust cases ever filed. *United States* v. *International Business Machines* was dismissed; *United States* v. *American Telephone and Telegraph* was resolved by a proposed modification of the 1956 consent decree. Today, this committee exercises its oversight powers to examine these actions taken by the Department of Justice.

Since the case against IBM is over, we will limit our inquiry to why the case was dismissed. The AT&T settlement is, however, a different matter.

In 1974, the Congress passed the Tunney Act. The provisions of the act set forth safeguards involving both public and judicial scrutiny of antitrust consent decrees which end litigation between the Government and private parties. The Tunney Act insures that Government antitrust cases are not settled by secret agreement.

Since the agreement between the Department of Justice and AT&T was announced on January 8, one question has been continually raised: Is the agreement subject to the Tunney Act? Will the public have an opportunity to review and comment on the agreement? Will the court have the power to accept or reject the agreement depending on whether it is in the public interest?

As of today, it would appear that Tunney Act procedures will be used to thoroughly examine the proposed settlement. Both the Government and AT&T have publicly committed themselves to this course. In my opinion, it is the course dictated by commonsense and good judgment, and it must be followed in every detail.

As is evident on its face, the AT&T agreement constitutes only an outline of the largest corporate divestiture in history. Even after the proposed modification is approved by the court, we will not know for 6 months the precise shape of the new and dramatically different telecommunications industry. A great many questions about the divestiture and its effects remain to be answered.

It is, therefore, entirely appropriate for the committee to explore the ramifications of this agreement. I can think of nothing more important than examining the effect of this settlement on local telephone rates across the country.

The debate on this sensitive issue began immediately when the settlement was announced. Some predict local rates will double or even triple within a very short time; others argue that local rates will be minimally affected by the court action, and any increases that do occur reflect inevitable market influences. Regardless of which position is correct, one thing remains absolutely clear: Telephone service must not become a luxury item available only to a comparative few. As chairman of this committee, I will work to insure that local rates remain reasonable and affordable to the general public.

Today, we shall explore numerous questions raised by the agreement, including its effect on the relationship between Federal and State regulation of communications, the dividing line to be drawn separating AT&T from local operating companies, and, of course, the existing need for telecommunications legislation. Time will obviously not permit the committee to explore all of its concerns at this hearing. Consequently, the record shall remain open for a reasonable time to permit committee members to submit written questions to our witnesses. It may also be necessary to conduct further hearings examining the agreement.

Professor Baxter, we are pleased to have you with us to discuss how the Department of Justice handled these two monumental cases. During your brief tenure in office, you have managed to bring to final resolution matters which have been pending for many, many years. I have often expressed my concern about the fact that antitrust litigation tends to go on indefinitely, consuming vast amounts of both private and public resources.

Regardless of how one might feel about the merits of either case, I believe it is admirable to have made some end to litigation that many had feared would be interminable. We must be sure, of course, that such resolution is in the public interest.

Senator Metzenbaum, do you have an opening statement you would like to make?

OPENING STATEMENT OF SENATOR HOWARD METZENBAUM

Senator METZENBAUM. Mr. Chairman, I want to commend you for holding this oversight hearing so promptly. I think it is significant and important. We in the Congress have responsibility to see that our antitrust laws are vigorously enforced.

This hearing to review the administration's latest actions comes none too soon. Settlement of the Justice Department's suit against AT&T took just about everyone by surprise. As a matter of fact, Mr. Baxter, you did so well in keeping it secret that maybe the

President should consider putting you in charge of plugging leaks, instead of running the Antitrust Division.

I think it is fair to say that the ramifications of the proposed settlement in this enormously complex case are still being examined and will be for some time. We must give Judge Greene credit for refusing to rubberstamp the agreement. It was a difficult position to put himself in. I commend him for recognizing the public interest in this matter.

Particularly in a case as complex as this, it is essential for all interested and knowledgeable parties to have a chance to analyze the settlement's implications. I am pleased to see that the settlement agreement will be thoroughly scrutinized in the courts, and I am pleased to see that my colleagues in the House and Senate recognize the need for congressional oversight of this extremely important matter as well.

There are some real questions in connection with the settlement that must be answered. The one that is probably the most important of all is, how does the proposed settlement impact on the consumers? Will residential consumers end up paying more for their telephone service as a result of this settlement? Will the quality of service deteriorate? Will the divestiture be structured in such a way that the local operating companies will be healthy and viable or will AT&T be able to remove the guts from the present operating companies, leaving them no options but to seek back-breaking rate increases from consumers in order to stay afloat?

Second, how does the settlement impact on AT&T's competitors? Our antitrust laws are designed to insure that our free enterprise system works well by seeing to it that there is effective competition. Does the proposed settlement insure a sufficiently competitive environment in all of the markets AT&T will now be permitted to enter?

What are the ramifications of unleashing a mammoth and, what Mr. Baxter would like to see, a totally unregulated AT&T, on the rest of the economy? Who will take on the responsibility of monitoring this monolith's market behavior? Or will AT&T be able to crush its competition before any antitrust enforcement agency even blinks, with a real question as to whether or not the antitrust enforcement agencies were even watching. These are all questions that should be asked at the hearings today and in the future.

In the past 2 weeks we have seen an amazing turnaround in three very significant Government antitrust cases. It is not alone enough to dismiss antitrust cases because they have been dragged through the courts for years. That is not an adequate basis to dispose of litigation. That relates directly to the question of how the Department, the defendants and the courts have acted in handling those cases.

As a matter of fact, the chairman and I both sponsored and saw through to passage the Antitrust Procedural Improvements Act in the last session of Congress, so that there could not be these interminable delays. But the delays alone would not, and should not, have provided a basis on which to dismiss the cases. That, in effect, would say that, if you have the wherewithal to hire the most expensive lawyers who know the best procedural steps to take in

order to use effectively a court kind of filibuster, then you never need to worry about effective antitrust enforcement.

Three of the largest and most important antitrust cases of the past decade have either been settled or dismissed within the past several weeks. In addition to AT&T, the Justice Department dismissed the *IBM* case, and the Federal Trade Commission dismissed its shared monopoly cereals case. What are the American people to interpret from that kind of action?

The latter two case dismissals seem to have gotten lost in the shuffle. Very little has been said in the media about it because all of the attention has been directed to the AT&T settlement. Frankly, that is very unfortunate.

I think we have an obligation to scrutinize these decisions as well. Again, the two essential questions with respect to these cases are: What will be the impact on the consumer and what will be the impact on competition?

Frankly, I have reached no conclusion about whether the decisions in any of these cases were appropriate, but I certainly have many questions in my mind. That is the reason I think it is so important that this committee investigate. If consumers are going to be burdened and if competition is going to be stifled rather than encouraged, then we have a case of our antitrust laws working in reverse. I, for one, do not intend to sit idly by while that happens.

None of us can afford to take our antitrust oversight responsibilities lightly. We must find out whether we are seeing vigorous antitrust enforcement or whether we are seeing anti-antitrust enforcement.

I might add that I have another set of related concerns about the AT&T settlement. I think that we must ascertain what the impact of the settlement will be on the AT&T employees themselves. Will their concerns about job security and retention of benefits be taken into account in the restructuring? Who will take on the responsibility of seeing that those concerns are met, or will those concerns be discussed and looked into by anyone at any place?

I believe that to be a very important factor in our oversight hearings. I believe it to be an important factor that I hope the court will take into consideration in looking at the settlement agreement. I hope some of the witnesses today will be able to enlighten us on these issues as well.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator.

Professor Baxter, we are glad to have you with us. You may proceed now.

STATEMENT OF WILLIAM F. BAXTER, ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE

Mr. BAXTER. Thank you very much, Mr. Chairman.

I have submitted a fairly lengthly statement to the committee discussing both the *AT&T* and *IBM* cases. I will not repeat it in its entirety. However, I would like to make a brief statement, and then I would propose to address myself to such questions as the committee may have.

The CHAIRMAN. Without objection, your statement will be made part of the record following your oral presentation.

Mr. BAXTER. I am grateful for the opportunity to come this morning and discuss the disposition of these two cases. Plainly, the dispositions of these two cases are the most important actions I have taken since I assumed my present position. Quite frankly, I am pleased with the disposition in both instances. That, I assume, goes without saying, and yet they are of enormous importance and it is entirely appropriate, and indeed helpful, I think, to the American people, that the committee should interest itself in these two dispositions.

Turning first to the AT&T matter, it is my view that our resolution of that case with the proposed modification to the old decree will bring about a new structure of the telecommunications industry that I expect to improve its performance and it will remit to the competitive sectors of our economy a large amount of activity which heretofore has struggled in the shadow of regulation.

Everyone should understand the technical details of what we have done. Until January 8, we were carrying on litigation with AT&T on two different fronts. One of those fronts was the antitrust case commenced in 1974 in the Federal district court in Washington. That case was late in the trial stages and probably could have been brought to conclusion by this summer.

However, there was a second front of activity pertaining to an earlier consent decree that had been obtained against AT&T. To understand what was going on in that case, one must also make reference to the decision of the Federal Communications Commission in its *Computer II* decision. There the FCC authorized AT&T to engage in a variety of potentially competitive activities if it did so through a fully separate subsidiary.

The 1956 consent decree, however, stood in the way of implementing the FCC's decision. Accordingly, the telephone company asked Judge Biunno in New Jersey for an interpretation of that decree which would authorize it to engage in these other activities. Judge Biunno had entered an order in response to that request, and his order had been appealed to the third circuit.

If this case was to be disposed of in any satisfactory way, it was necessary to bring the 1956 decree case into harmony with any proposed outcome in the 1974 case because, quite plainly, that decree had a very important bearing on the business conduct of the telephone company. Accordingly, when we were able to work out an agreement substantively, we adopted a particular procedural vehicle for getting both those cases in front of one judge and putting him in a position to dispose of them comprehensively.

Judge Greene had done a magnificent job, as Senator Metzenbaum indicated a moment ago, of trying the 1974 case, moving it along quickly. It was clear that he had acquired a thorough and detailed understanding of the industry. Accordingly, the first determination that I made in my own mind was that the entire problem should in some way be brought before Judge Greene. In order to do that, it would be necessary to transfer the 1956 decree down to Judge Greene's court. With a view to making that possible, we took a number of steps.

First of all, we dismissed the appeal that was pending from Judge Biunno's order in the old case. Second, we filed our agreement as a proposed modification to the decree in the old case. Third, we jointly filed a motion with Judge Biunno to transfer the old case down to Washington. Having put the matter before Judge Greene in that form, we dismissed the 1974 case and, thus, we have arrived today at exactly the posture I stated that I intended to bring about when I made the announcement of our decision on January 8.

The whole matter is now before Judge Greene in the Federal District Court for the District of Columbia. It is before him in the form of a proposed modification to the 1956 decree. He is familiar with the circumstances of the industry at the present time.

As we announced at the outset and have always intended, there will be full publication of the proposed decree, hearings on the proposed modification at which parties will have an opportunity to make their views known, and Judge Greene will have the power to accept or reject the modification in accordance with his perception of the public interest.

As for the technical question of whether the Tunney Act applies, it is my view that it does not. This is not a consent decree; it is a proposed modification. Of course, it is a proposed modification of enormous importance. Because it is of enormous importance, it seems entirely appropriate to me—and it has always been our intention—that we would follow procedures which precisely parallel the procedures of the Tunney Act.

On the other hand, most modifications of outstanding consent decrees involve very minor problems, technical adjustments which are of interest to no one except the Government and one private party. I think it would be a great waste of the resources of the Department and of the judiciary if we were to accept the rigid position that every modification, however trivial, called into play the full array of Tunney Act procedures.

Complying with those procedures is very, very expensive. Publication costs alone sometimes run into the hundreds of thousands of dollars. That is quite appropriate where what is being proposed is of great public interest, as it is in this case, as it frequently is in the case of consent decrees, but it certainly is not in the context of the preponderance of modification orders.

Thus, we take the position that the Tunney Act does not technically apply because this is technically a modification and not a consent decree, but at the same time we propose to follow the procedures called for in the Tunney Act in all their detail. Accordingly, the case is before Judge Greene in that posture.

The decree itself calls for a separation between the basic operating companies on the one hand and the other facilities of the AT&T company. The decree leaves open the question of whether there will be 1 basic operating company, 5 regional operating companies, 10 regional operating companies, or some other number.

That does not mean that it is left wholly within the discretion of AT&T. They are required to file a plan of reorganization which requires approval. The FCC, of course, has the jurisdiction conferred upon it by the 1934 act and may, like other parties, have views on that or other matters they may wish to file with the court. We, of

course, would take those views very much into account in view of the expertise the FCC has accumulated with respect to this industry over the years.

The definition of a basic operating company is contained in an appendix to the decree. Basically it includes all those facilities which are necessary to originate and terminate local calls through an exchange area, and also the trunking leading beyond the end offices up to what is in present AT&T terminology called the class 4 switches, the point at which, in accordance with the definitions of the decree, the interexchange function commences.

In working out that definition, it was my purpose to try to ascertain as precisely as we could where the natural monopoly function performed by the local telephone companies began and ended. The critical point is how much of the telephone company's facilities should competitors who wish to compete in long distance service have to duplicate. It was my view that they ought not to have to duplicate anything closer to the ultimate telephone user than the class 4 switch.

There are a variety of provisions in the decree which require the local operating companies, thus defined, to deal on an equal basis with the to-be-separated AT&T company and competitors of the AT&T Co. Henceforth, there will be competition in the provision of equipment, the sale of equipment, to the local operating companies; in the provision of long distance services to the local operating companies; and, indeed, in the provision of all other products and services that the local operating companies may need.

After the separation occurs, I would expect that the self-interest of the local operating companies and of their officers would lead to a nondiscriminatory result, even without the existence of those provisions. They will have every incentive in the world to seek the best products at the lowest costs that they can find.

The separation, of course, cannot be made to occur instantaneously. There is an interim period which by its own terms may last as long as 18 months from the date on which the modification is entered by the court. It is during that interim period that these antidiscrimination provisions are of particular importance. Those provisions go into effect with the filing of the decree.

The local operating companies will, of course, remain subject to the regulation of the public utility commissions of the various States in which they exist. In various respects, both the basic operating companies and the AT&T Co. will remain subject to the jurisdiction of the Federal Communications Commission. Those regulatory agencies will continue to have an active role to play in the future, as they have in the past.

I am sure you will have many more questions. Some have already been suggested. However, at this point I think I will turn, if I may, to our actions in the *IBM* case.

Unlike the *AT&T* case where I regard the settlement at which we arrived as a very, very substantial victory for the Division and for the American people, in IBM we simply acknowledged defeat and dismissed the case.

I started reviewing the *IBM* case this summer. I was aware, of course, of its long and tangled procedural history. I was aware of the many private cases that had been brought against IBM, more

or less in the wake of the Government's case against IBM, but I did not have any particular view of the merits or demerits of the IBM case itself. The record there is enormous in its proportions, and attempting to familiarize myself with it was not a minor task.

Over the months of late summer and early fall I read reports that had been prepared within the Division on the *IBM* case. I held meetings with my own trial staff at which they reviewed for me the evidence that was in the record on the critical issues. I held meetings attended both by my own trial staff and by the IBM trial staff, which were conducted more or less as seminars for my benefit with the opposing sides arguing the strengths and weaknesses of the record on these critical points. I read portions of the record itself, not all of the record to be sure—that would have taken a very, very long time—but portions of the record on issues that I regarded as critical.

I would like to review for the committee briefly the substantive conclusions at which I arrived as a consequence of that process of review.

The *IBM* case was brought on the theory not that IBM had obtained its very large market share through improper practices, but that it had maintained that large market share through improper practices. There were really three basic questions to be answered. The first was: Is there an economically significant market within which IBM does have so large a market share to be able to reach the conclusion that it is a possessor of a monopoly position within the meaning of section 2?

If the answer to that question is yes, the next question is posed: Did IBM engage in legally unacceptable behavior with respect to that market? If the answer to that question is yes, then the third question is: Is there a causal connection between the inappropriate behavior in which IBM engaged and IBM's maintenance of its dominant market position?

My conclusions with respect to those three issues were as follows:

With respect to the first question, although there were real problems with market definition, I think it could fairly be said that IBM at various points of time, including perhaps the present, has had a significantly large market share, a sufficiently large market share to bring the operation of section 2 into play.

Exactly how large that market share is is quite sensitive to precisely the way one defines the market. Basically, the Government's alleged market definition in the *IBM* case was computer systems, not just the mainframe processor, not just the mainframe processor with its associated operating system and other software, but the entire system, including the various input/output devices and associated memory that are attached to it.

The market definition was large computer systems optimized for business use. That was to distinguish the market which the Government was alleging so that it did not include the very large scientific machines, the so-called number crunchers, that are used predominantly in scientific as opposed to business facilities.

Whether that is really a permissible separation between systems optimized for business use and the large scientific machines I think is a serious question. Furthermore, there is the question: How large

is large? As one drops down CPU size even a little bit, one finds that IBM's market share starts to get smaller quite rapidly.

Finally, there was the question: How do you measure IBM's market share? Do you look at the question of installed base—how many machines are out there that originally were manufactured by IBM—or do you look at the annual sales, which is more nearly what we do in most circumstances? Again, IBM's market share tended to be larger if you looked at installed base than if you looked at annual shipments.

Nevertheless, however one looked at it, IBM has and has had a very large market share. I can produce responsible calculations of that market share that vary anywhere from slightly more than 50 percent up into the high 70-percent ranges. This was not a reason to dismiss the *IBM* case.

I go on to the second set of issues: Did IBM engage in improper practices with respect to this market? There were very serious problems there. There were in the record two, or perhaps three, credible episodes for which criticism might be directed at IBM. I will talk about one which I regard as far and away the most persuasively supported of those episodes.

This episode occurred in the late sixties with respect to a computer system or a subset of a computer system known as the 360/90. In the early to mid-1960's IBM brought into existence a computer revolution by creating an entire family of computers, the 360 family, with its own operating system and very, very important interchangeability features, so that one could move from a 360/40 to a 360/50 or any of the other members of the family without the enormous expense of reprograming application software and so forth.

There came a point in time when IBM realized that it was falling behind the leaders of the technology in the very largest of those machines, a scientific machine, and it made a decision to go ahead and build and market the 360/90.

I think the record supports fairly persuasively the conclusion that IBM knew it would never recover the costs of the 360/90. In short, one could look at the episode involving the 360/90 as involving predatory pricing. IBM did build the machine, market the machine, and it lost a great deal of money doing that.

On the other hand, one could look at the 360/90 story in a rather different way, simply as IBM's recognition that it had to keep its hand in the large scientific machine market; that it had a lot of learning to do there; and that even if the machine itself or the individual copies of the machines it was able to sell did not recoup the cost of the entire program, that the program, nevertheless, represented a sound investment in the future.

Nevertheless, as I say, the record would have supported, arguably at least, the conclusion that the 360/90 represented an instance of predatory pricing.

The real difficulty with the 360/90 story—and indeed the several other episodes to which I have referred and on which I would be happy to elaborate, should the committee wish more detail—the real difficulty is that the behavior could not plausibly be asserted to bear any causal relationship to the maintenance by IBM of its

large market share of the business optimized market that the complaint alleged.

The 360/90 was not in the market that the Government alleged to have been monopolized. It was precisely the large-scale, scientific machine that the Government was at pains to exclude from the market it claimed to be monopolized. Furthermore, IBM's effort at predation, if indeed it can so be characterized, was spectacularly unsuccessful. IBM succeeded in selling only 12 or 14 of those machines.

At the very same time, the competitor, Control Data Corp., at which this predatory effort would necessarily have been aimed, should it be regarded as a predatory episode, managed to sell over 200 machines that were direct competitors with the 360/90. So that even if one would be correct to regard this as an episode of predation, it was wholly unsuccessful viewed as such an episode, and it was aimed, if it was aimed at anyone, at a competitor who was not in the market IBM was alleged to have monopolized, and failure is complete at the level of causality.

Unless the committee indicates that it wishes me to do so in its questioning, I will not go into the other episodes in any detail. Again in that context, I would say only the following: Like the 360/90 episode, each of the other episodes was not really involved in the market that IBM was said to have monopolized.

Having reached that conclusion, I was faced with the question: What then should be done? It is true that the liability phase of the IBM case was within a few months of submission to the judge. There would then be a very, very long hiatus while the judge attempted to cope with that very, very large record and come in with some sort of findings.

Perhaps we would have lost at that stage; certainly in my view we should have lost at that stage. If, on the other hand, we won, what then? There had been no relief hearings in IBM. Another extended proceeding before the Federal district judge with respect to relief would have been necessary. More discovery would have been necessary because relief, of course, must be forward-looking and must have its orientation in the industry as it is today, not the industry as it was in the late sixties and early seventies. That is when the record in the IBM closed, as of 1972, I believe. Extensive discovery and litigation with respect to remedy would have been necessary had we won on the liability phase.

If we succeeded in obtaining any significant relief at the end of the remedial stage—4 or 5 years from now would have been an optimistic view of when we might have enjoyed that success—appeal by IBM to the second circuit was absolutely inevitable. We would have been looking forward to several more years of proceedings before——

Senator HATCH. You are talking about 20 years of one case in the Federal courts, approximately?

Mr. BAXTER. From beginning to end it would have been at least a minimum of 20 years.

Senator HATCH. That is incredible.

Senator METZENBAUM. Did the Justice Department ever go into the court and ask the court to set up a procedure to expedite the case?

Senator HATCH. If the truth is known, did not the Justice Department actually continue to say that they could not even complete the case for 5 or 6 more years on the district court level?

The CHAIRMAN. Gentlemen, I think we had better follow the usual procedure and let Mr. Baxter finish his statement, and then we will proceed with the questions.

Senator HATCH. Could he answer those questions, though—Senator Metzenbaum's and mine?

The CHAIRMAN. Answer those questions, and then we will proceed in the usual manner.

Mr. BAXTER. Senator Metzenbaum's question was: Did the Justice Department ever go in and ask the judge to expedite? That is a very difficult question to answer.

Both the Justice Department and IBM represented that a great deal of its efforts were intended to expedite and to assist the judge in expediting the case. Somehow or other, the case never got expedited. I think it is difficult to say in retrospect where primary fault for all the delay lay.

However, I have no difficulty saying that as I review the procedural record—and I should add that my review there is much more cursory than my review of the substantive record—I have no difficulty identifying respects in which I would lay blame at the feet of all three of the participants: The context in which, it seems to me, the Justice Department greatly complicated and delayed the conclusion of the case; the context in which IBM did so; and the context in which the judge, simply by bad management, failed to expedite the case.

The CHAIRMAN. Do you want to answer Senator Hatch's question?

Mr. BAXTER. Senator Hatch's question, I assume, is: How long would the case have lasted overall if we had gone ahead?

Senator HATCH. And the fact that the Justice Department continued to ask for delays, I suppose in part because they would file 1,800-page interrogatories and other extensive pleadings that always had to be reduced to reasonable form, which looks like the almighty power of the Federal Government was being used to oppress rather than to resolve these problems; thus, continuing the case, elongating the case, extending the case, so that the three issues that you are mentioning here today really could never be arrived at. Then, as I recall, they came into court and asked for another 6 years, telling them that they could not even be ready for trial for another 6 years.

Am I wrong on that?

Mr. BAXTER. You may remember the procedural history in those early phases better than I do, Senator.

Senator HATCH. But I am pretty close to——

Mr. BAXTER. There was a great deal of that; that is true.

Senator HATCH. Therefore, you would agree with at least the general characterization?

Mr. BAXTER. The case was not tried expeditiously. The issues were not sharply framed at the outset. The whole case should not have taken longer to try than the *AT&T* case.

Senator HATCH. Mr. Chairman, if I may just add something—this case personifies what many people in the private sector feel is the

oppressive power, an arm of the Federal Government extending cases beyond reasonability. Actually, had it not been IBM but had it been some other private sector company, it could not have lasted; it would have been broken by this kind of case. That is probably true, is it not?

Mr. BAXTER. I think that incompetence—that is a harsh word, but a softer substitute does not come readily to mind——

Senator HATCH. I think it is a very good word in this case.

Mr. BAXTER [continuing]. Played a larger role than the malice and oppressiveness that you seem to be suggesting by your comments.

Senator HATCH. No; I am suggesting incompetence. I also am suggesting politics.

Senator METZENBAUM. Mr. Chairman, I am perfectly happy to sit here and be cooperative, but if the Senator from Utah is going to continue to make political speeches, I want equal time.

Senator HATCH. Well, you always take as much, if not more, on political speeches as I do.

The CHAIRMAN. I think we had better go ahead with the regular procedure, allowing so much time to each individual to ask questions.

Are you through with your statement, Mr. Baxter?

Mr. BAXTER. I am, Mr. Chairman. I would be happy to respond to questions.

The CHAIRMAN. He is through with his statement. Then I think we had better proceed in the regular fashion.

Senator HATCH. May I just take a couple minutes, with Senator Metzenbaum's indulgence?

The CHAIRMAN. Go ahead.

Senator HATCH. What bothers me is, like the shared monopoly cases which you also have had basically to withdraw, this case——

Mr. BAXTER. I did not have any shared monopoly cases, Senator.

Senator HATCH. I am not blaming you for it; I am saying that you have acknowledged, as I understand it, that shared monopoly may have been more than esoteric theory in the field of antitrust. I think you have brought some balance to the field of antitrust. I want to compliment you for it.

One thing that is very difficult for Government lawyers to do is to admit that maybe they have been wrong or maybe in the past there has been some incompetence or maybe in the past there has been some oppression. Even though IBM can afford to defend this kind of case, not many other companies in this country could afford to go through what has been in essence—what is it, 11 or 12 years——

Mr. BAXTER. Thirteen, I believe.

Senator HATCH [continuing]. The years of litigation with the Government coming in and saying it probably needs another 5 or 6 years just to get ready for trial, and then the appeals and everything else.

My concern is that antitrust laws ought to be enforced. If IBM broke those laws, then IBM ought to pay the consequences, and the Government should expeditiously bring a competent case and resolve that in the interest of the consumers of America.

I will just ask you one question with regard to AT&T. What result will the settlement of the *AT&T* case have with regard to the Packwood bill and the Wirth bill in the House, and perhaps an ultimate legislative resolution of this matter also? What would be your recommendation? Would your recommendation be that the settlement agreed to by the Justice Department and AT&T—and hopefully, in the eyes of both, by Judge Greene after public comment—if that is agreed, would that be a definite, final, and good resolution of the problem or should we still push legislation to try to resolve this problem further?

Mr. BAXTER. I would respond by saying neither of the above, Senator. My own recommendation would be that the Congress adopt a wait-and-see attitude for 6 or 8 months at least, until we see what that divestiture plan really looks like.

It is quite clear to me that this decree, if it is entered as a modification, so substantially changes the telecommunications industry that the provisions of S. 898 are simply irrelevant to the industrial situation which will then exist.

The divestiture which is contemplated by the proposed modification substantially solves most of the problems, but not all, at which S. 898 was addressed. At a rough guess, I would say that 90 percent of the words in S. 898 were addressed in one way or another to the problem of cross-subsidization between the regulated and unregulated sectors, and that problem is now simply put to rest in all but one minor respect.

The minor respect, of course, is that the Long Lines Division of AT&T will continue to be regulated by the FCC for some period of time. I can imagine the Congress wanting to take a look at some interim provision there. I can imagine the Congress wanting to look at a variety of residual problems that may characterize the industry after the decree goes into effect.

However, I think we all would be in a much better position to say exactly what is needed and to work on whatever constructive legislation may be needed to amend the 1934 act, which definitely needs updating, after we know a little more about what this industry will look like in the years ahead.

Senator HATCH. During your testimony before this committee on the telecommunications bill you indicated that the opportunity existed for AT&T to cross-subsidize the fully-separated affiliates which the bill would have allowed. What opportunities would exist, after the pending settlement, for AT&T to cross-subsidize its competitive offerings through its regulated long distance services?

Mr. BAXTER. Very little, I think, Senator. I am not nearly so concerned about that as I was about the potential for abuse of the bottleneck facility at the local BOC level. There you really did have a powerful, natural monopoly, an enormously powerful, natural monopoly that also enjoyed statutory entry barriers in most areas.

It is perfectly true that after divestiture occurs the Long Lines Division of the AT&T company will continue to have a very large market share of long distance service. At the present time it has over 90 percent, and that percentage will not drop immediately.

There is, however, no statutory entry barrier. There are powerful and well-financed potential competitors out there who are already competitors in some respects. The equal treatment provisions of the

decree will assist them in entering these long distance markets. I do not believe that AT&T will have substantial market power to operate as an engine of cross-subsidization, notwithstanding that it continues to have a substantial market share. Substantial market share and substantial market power just are not identical phenomena.

Although the surviving AT&T company will tend to have a very large market share, I do not think, except perhaps in the very short run—and I am not even sure about the very short run—there is really need to worry about extensive cross-subsidization out of the Long Lines Division.

Senator HATCH. Then, in your opinion, should Congress establish any safeguards to ensure that cross-subsidization does not occur?

Mr. BAXTER. I think that problem is largely solved. However, to the extent there is a problem, that Congress should reach the conclusion there is a problem, it would be with respect to the Long Lines Division, and then only for a short period of time.

Senator HATCH. Thank you, Mr. Baxter. I appreciated your testimony. I appreciate the tremendous problems that you have in some of these cases and at least the attempt to provide some leadership in this area and resolve these problems one way or the other.

I wish you success in this matter because it looks to me as though it may be a breakthrough that might cause a solution to some of these major problems that have existed for years because I think of a lack of leadership in this area. I commend you for that.

I also thank you, Mr. Chairman and Senator Metzenbaum, for allowing me to go first.

I appreciated hearing your testimony today.

The CHAIRMAN. Since these questions relate to each other, and inasmuch as there are only two of us here, I will probably take about 20 to 25 minutes to conclude my questions with you and then turn the questioning over to Senator Metzenbaum. In that way, neither one of us will be interrupted in our thoughts.

Both the Department and AT&T have expressed a desire for Tunney Act procedures to apply in the proposed modification of the 1956 decree. At the same time, however, both parties have requested the court to dismiss the 1974 suit. It seems to me that Tunney Act procedures could be effective only if the court had an existing lawsuit to fall back on if the modification proved unsatisfactory. If the 1974 case is dropped, the option of resuming the trial no longer exists. Do you agree with this analysis?

Mr. BAXTER. I really don't, Mr. Chairman. The 1974 case was dismissed without prejudice. If the court should reject the proposed modification of the 1956 decree, it can be resumed.

The CHAIRMAN. Under the proposed modification, AT&T is to submit its reorganization plan to the Justice Department for its approval. How much flexibility will the Justice Department have in negotiating the terms of the plan and is it your intent that the plan be subjected to the Tunney Act requirements just as the proposed modification will be?

Mr. BAXTER. We certainly would make the proposed plan public and welcome comments on it. Obviously, we will look at it very, very closely ourselves. Whether one would wish again to track the hearing requirements and some of the other features of the Tunney

Act proceedings is not a decision that we have made at this point. I do not mean to rule it out, but certainly I do not contemplate that approval of the plan would occur in the quiet of my office without an opportunity for parties who are interested to make their views known.

The CHAIRMAN. Mr. Baxter, why did AT&T and the Justice Department agree in the proposed consent agreement not to give Congress access to data obtained during the course of securing compliance with the settlement?

Mr. BAXTER. I am sorry, Senator, I am not sure I understood that question. I do not believe there is anything in the agreement that says that we won't.

Senator METZENBAUM. It is in section VI(b).

The CHAIRMAN. I believe it says it would not be made available to anyone except the executive branch and the FCC.

Senator METZENBAUM. It is in section VI(b) on page 12 of the agreement. It says, "No information or documents obtained by the means provided in this section shall be divulged by any representative of the Department of Justice to any person other than a duly authorized representative of the executive branch of the United States or the Federal Communications Commission except in the course of legal proceedings to which the United States is a party or for the purpose of securing compliance with the final judgment or as otherwise required by law."

That very obviously excludes Congress.

Mr. BAXTER. Yes. That is really a fairly routine provision I think. I had forgotten that we had even put it in there in the sense that it was not part of what I was negotiating for a long period of time, but more or less the incorporation of standard provisions. Indeed, in large part that reflects existing obligations to keep material confidential.

The CHAIRMAN. Was that to protect confidentiality or for some other reason?

Mr. BAXTER. That is, as I say, a fairly routine provision that was intended to protect confidentiality of material that we had obtained from the AT&T company.

The CHAIRMAN. Professor Baxter, I think that one of the most important questions I have about the substance of the proposed modification is its expected effect on consumer telephone rates. In your opinion, will divestiture of Southern Bell as well as the other BOC's result in higher rates for private consumers, and in particular for consumers in rural areas?

Mr. BAXTER. I have a confident answer to that question, Mr. Chairman.

The CHAIRMAN. I cannot hear you. Please speak up.

Mr. BAXTER. I have a very confident answer to that question. That is that the modification or decree, if it becomes a decree, will have no effect whatsoever one way or the other on local telephone rates. Now let me explain some of the features that go into that answer.

At the present time one has to keep in mind that there are a number of fund flows between the local operating companies and the AT&T company.

Senator METZENBAUM. What was that word? There are a number of what?

Mr. BAXTER. Fund flows. Flows of funds.

Senator METZENBAUM. Fund flows. OK.

Mr. BAXTER. In the first place, the local operating companies pay a license contract fee to the AT&T company, a certain percentage of their revenues in exchange for certain central management services and for access to Bell Laboratories research.

In the second place, the local operating companies buy the overwhelming preponderance of all their equipment from the Western Electric Co. Again, there is a big fund flow in that source.

Finally, there is a process called "separation and settlements" that occurs. If one thinks about the local operating company, one can conceive of it as performing two quite different functions with one set of equipment. With that one set of equipment and switches, it both originates and terminates local telephone calls. At the same time, all long distance calls originating or terminating in the exchange area go through those same switches and over those same lines.

It is necessary to allocate the costs of local telephone service—or I should say the cost incurred by the local telephone companies—alternatively to local telephone service or long distance telephone service. Now many of those costs are strictly dependent on the number of calls and the length of the calls, and some costs can be allocated on the specific basis of how much traffic was there, how many local calls were there, how many long distance calls were there.

However, with respect to large portions of that equipment that is not possible. You simply have to have the equipment to do either one. Once you have the equipment, you can do both. This portion of the equipment in the argot of the telephone industry is referred to as "nontraffic-sensitive costs."

The separations and settlements process, or the separations process, makes that cost allocation. The people who claim that local telephone service is being subsidized to some extent by long distance service in effect are expressing the view, although they very rarely put it this way, that the separations process comes out very favorably to the local company; that more costs are allocated to the long distance than in some sense ought to be; and that this helps keep local rates down.

It is perfectly true that the decree eliminates, or certainly drastically alters, these three fund flows. It eliminates payments under the license contract entirely. It eliminates the settlements process. It creates the opportunity for local operating companies to buy the best equipment they can find at the lowest prices at which they can find it, so it may affect that fund flow, too. Indeed, I think it will.

How those three things balance out is a matter of judgment. I do not mean to express any confident judgment on it.

However, now I want to bring into the picture one more and new fund flow that is created by the decree. That is what the decree refers to as access charges or access tariffs.

In the future the local telephone company will charge the long distance carrier, whoever that may be, a fee for originating or ter-

minating the long distance call. The local telephone company will publish tariffs that announce what those fees will be. In constructing those tariffs one will look to the local properties and ask, what fraction of the costs of these local properties, local equipment, shall we attribute to long distance service? In short, in the future the process of constructing the access tariff will take the place of the present settlements process.

Now if one thinks it is appropriate, if the relevant regulatory agency wishes to build a subsidy in there to keep local phone rates down and to keep long distance rates high, the exchange access tariff is a vehicle that is available and through which that can be done.

By making the same heavy allocation of cost to the long distance service that is presently made, if indeed it is presently made, in the separations process, one can produce a system that generates quite high exchange access tariffs and creates whatever level of subsidy is desired—the present one, a greater one, a lesser one.

The relative costs of long distance service and local service are wholly unaffected by the decree except to the extent the decree creates a mechanism which puts that relationship in the hands of the regulatory agencies. In the future, as in the past, they will essentially be able to create any relationship they wish in those respects.

The CHAIRMAN. Professor Baxter, after divestiture it appears that AT&T will retain the yellow pages directory service. Wouldn't it be advisable to leave this lucrative business with the BOC's to help defray any increase in the cost of local service?

Mr. BAXTER. Senator, there has been a fair amount of misunderstanding with respect to the so-called yellow pages. Let me try to answer your question by urging you to look at it in a slightly different way.

After divestiture, the local operating company should not be engaging in any potentially competitive activities. Publication of the yellow pages is a potentially competitive activity. McGraw-Hill or AT&T or Fawcett Publications—or I can think of a long list of possibilities—may wind up publishing the yellow pages.

However, nothing can change the fact that the local telephone company as part of its natural monopoly is the only entity that starts off with a machine-readable set of local listings. Now it is that machine-readable set of local listings that underlies the profit that we associate with publishing the yellow pages.

In my conception, after the separation occurs, the local telephone company will—I am going to use the phrase—auction off to the highest bidder the exclusive right to have access to its machine-readable set of local listings for the purpose of creating the yellow pages.

Someone else will sell the display advertising. Someone else will set the type. Someone else will run off the books and distribute them. However, since they will have to pay the local operating company to get at the essential underlying data, they will make only a competitive rate of return on the activities they perform. There will still be an enormous revenue-generating potential in the fact that the local operating company has the exclusive possession of this machine-readable set of listings.

Although someone else will be engaged in the physical activity of producing and distributing the yellow pages, all of the supracompetitive profit that is now associated with that activity will necessarily be captured at the local operating level and will not fall into the hands of whomever performs the activity, because competitive bidding will drain those funds out at the local telephone company level.

Senator METZENBAUM. Mr. Baxter, apropos of the chairman's question, it is my understanding that AT&T is going to retain in some way the right to publish the yellow pages. Are you saying to us that is a right that will be in the hands of the BOC's and that they will have the right to sell the rights to publish the yellow pages by selling the machine-readable listings? That is a total contradiction of what I understood to be the settlement agreement.

Mr. BAXTER. Your question has two pieces, and I cannot answer both pieces yes or both pieces no. Yes, I am telling you that the local operating companies retain the right to sell the underlying computer listing and that is what is really valuable.

In response to the first part of your question, does the local operating company retain the right to publish the yellow pages, no, they don't. The yellow pages will be published by someone else, maybe AT&T.

However, it is of enormous value, if one is going to attempt to publish yellow pages, almost indispensable, that you have the computerized listing of the local phone numbers. That will be in the hands of the local operating company to sell, negotiate—I said auction before. I do not care whether they auction it or whether they negotiate with a variety of different publishers to see who is willing to pay most in order to get that underlying computerized listing.

The profit that we associate with yellow pages today inheres in that computerized listing, not in the yellow pages as such.

Senator METZENBAUM. I am just trying to get this clarified.

The CHAIRMAN. Senator, we are going to have to proceed in some regular way. If you will let me finish—I stated we want to follow the normal procedure. That is the reason I am allowing more time this morning. The Senator from Pennsylvania has come in. We are allowing more time to each question, so that the trend of thought will not be broken. Then we will allow you any reasonable time.

Senator METZENBAUM. It was only clarifying the answer to your question.

The CHAIRMAN. You can ask him to clarify it when you ask him your questions. I want to get through my questions.

Senator METZENBAUM. All right.

The CHAIRMAN. Professor Baxter, do you have any concerns that high access charges to protect consumer rates might inhibit the ability of long distance carriers to compete with AT&T long lines?

Mr. BAXTER. No, I do not, Senator. If access tariffs are raised, thus implicitly imposing a surcharge on long distance telephone calls in order to subsidize local telephone calls, the tariffs will be the same—higher, to be sure, but they will be the same—for AT&T and AT&T's competitors, so that it should not interfere with the competitive relationships between the several long distance carriers. What is required under the decree is uniform access tariffs for

all interexchange carriers, and an element of subsidy can be built into those tariffs if the regulators choose to do that.

The CHAIRMAN. Professor Baxter, do you believe that long distance service should be substantially deregulated? If so, with what sort of a time table?

Mr. BAXTER. I do believe it should be substantially deregulated. I would not be prepared today to specify the time period. However, over some period of years—2, 5, 7, something on that order—I see no further need for the regulation of long distance service.

The CHAIRMAN. Professor Baxter, under the decree would AT&T be allowed to construct facilities to bypass the local regulated exchange carriers including the BOC's?

Mr. BAXTER. Under the decree, the surviving AT&T company becomes a competitive company, like IBM or Columbia Broadcasting Company or any of a variety of others. I have described the local telephone companies as natural monopolies of enormous power. The one vulnerability in that monopoly of enormous power is their vulnerability to being bypassed.

Technologically, at the present time that is not easy, but I think it is readily foreseeable that a day will come when it is possible to mount a small parabolic antenna on the roof of a building, including a residence, and to bypass the local operating company using microwaves or, conceivably at some point in time, laser technology. Yes, AT&T will be free to do that to the extent that IBM or CBS or Home Box Office is free to do it. Of course, in my view we should regard that as a welcome technological development, a victory of technology over another instance of natural monopoly.

The CHAIRMAN. Professor Baxter, the proposed modification does not seem to prohibit AT&T from reentering the business of providing local exchange services through means such as cable, cellular, fiber, optic, or satellite systems. Would such activities by AT&T raise any competitive concerns?

Mr. BAXTER. As long as the local operating companies are there to provide telephone service, they will impose a very, very powerful, competitive check on alternative technologies for providing local telephone service. Thereby, they will prevent alternative technologies—unless they are far beyond any technology of which we know at the present time in their costsaving potential—they will prevent these alternative technologies from being substantial generators of supracompetitive profits with the potential for cross subsidization.

Yes, the decree does not keep AT&T from doing any of those things. No, in the present state of technology—or any I can foresee over the next 20 years—that does not pose a significant problem.

The CHAIRMAN. Professor Baxter, do you envision that under the provisions of the proposed consent agreement AT&T will be able to retain its position as a dominant carrier in the telecommunications industry?

Mr. BAXTER. If AT&T makes good products and prices them at low prices, it will capture a very significant share of telecommunications business. It will have some significant competitors in that endeavor. However, assuming that it captures a very large market share simply by giving good products to its customers, why, we should all applaud it for doing so.

The CHAIRMAN. Professor Baxter, does the proposed decree anticipate AT&T's divestiture of Cincinnati Bell and Southern New England Telephone Company? If not, why not?

Mr. BAXTER. Those two companies are not presently more than 50 percent owned. There are only minority interests I think in those two companies. Therefore, they are not listed as subsidiaries within the meaning of the decree. Precisely how AT&T proposes to deal with those two affiliated companies I think is a question that would better be put to AT&T. Their representatives, I am sure, will be able to give a helpful response, more helpful than I, to that question.

The CHAIRMAN. Professor Baxter, do you believe that permitting Western Electric to remain in close association with Long Lines could result in competitive advantages to Western Electric with respect to information disclosure about such things as changes in protocols and technical interface requirements?

Mr. BAXTER. This, again, is a transitional problem. So long as Long Lines has a very, very large market share and so long as there is an affiliation, Western Electric probably will have something of an advantage in supplying Long Lines' needs.

On the other hand, it is not an exploitable advantage because if Western were to make inferior products or if it should price them high, why, it will force Long Lines' costs up and Long Lines will rapidly start losing market share to exchange carriers.

In short, so long as the Long Lines Division is subject to a powerful form of potential competition and some actual competition, that effect will flow back through the company to the Western Electric operation. I do not see that as a serious problem.

The CHAIRMAN. Professor Baxter, how will competitive manufacturers or independent telephone companies get technical interface information so their equipment can interface with the AT&T network?

Mr. BAXTER. Of course, in the future there will not be an AT&T network, precisely because of the separation. What they will have to interface with is the local operating companies since all messages must be both originated and terminated locally. In the decree the local operating companies are enjoined from treating other third party suppliers any less favorably than the to-be-independent surviving AT&T company. In short, they will make interface characteristics available to competitive manufacturers as soon as they are made available to the Western Electric Company.

The CHAIRMAN. Professor Baxter, why doesn't the proposed modification contain any of the provisions regarding the mandatory licensing of patents as were in the 1956 decree?

Mr. BAXTER. The 1956 decree contemplated that Bell Laboratories research would continue to be funded with monies derived from telephone ratepayers. Under those circumstances, it was thought appropriate that the fruits of that research should be available on a basis other than the usual commercial basis, which involves people getting proprietary patents on their inventions and being able to license them or not, as they see fit.

After the divestiture, the research in which Bell Laboratories engages will have to be funded by AT&T funds derived from Western Electric sales or from Long Lines' revenues. They will be propri-

etary funds of a competitive company. To the extent they are invested in research and fruitful in yielding patents, it seems to me that the interest in those patents should also be proprietary. I would not regard it as appropriate to continue the mandatory licensing provision under those circumstances.

The CHAIRMAN. Professor Baxter, how much difficulty do you think there will be in developing competition in the equipment market, given the close relationship that Western Electric has had with the BOC's for so many years?

Mr. BAXTER. There will be some inertial forces there probably, simply styles of thought that create a residual advantage for Western Electric for a period of time. However, those are not very powerful forces. They can be disrupted by competitors, and there will be competitors. One of the competitors may be the IBM Company. In some respects, I thought the most effective relief I could find in the *IBM* case was freeing AT&T from the 1956 consent decree, and in some respects the most appropriate relief in the *AT&T* case was freeing IBM from further harassment in that litigation.

The CHAIRMAN. Professor Baxter, the proposed modification expressly states that it does not require or prohibit the consolidation of the ownership of the BOC's into any particular number of entities. Does this indicate that you do not believe there would be any anticompetitive results in areas such as procurement, for example, if the BOC's were combined into one large company?

Mr. BAXTER. I do not think there would be a significant degree of monopsony power even if all the BOC's were combined. It is perfectly true that if they were combined they would be purchasers of a very large percentage of certain kinds of items, most importantly stored program switches, probably, in the future.

However, the reason there would not be significant monopsony power there is because from a technological standpoint there is so little difference between the stored program communications switch and a computer. One has to have trapped resources on the supply side in order to be able to exercise monopsony power, and there simply would be no trapped resources in this circumstance. So I would not view even a consolidation of all the basic operating companies into a single company with great alarm.

On the other hand, I would emphasize that the decree merely states that nothing in the decree prohibits or requires any particular combination, and, therefore, other sources of influence and legal obligation would continue to play a role. I can imagine that the regulatory agencies, or perhaps eventually the Congress, might have some views on that matter of how the BOC's were combined.

The CHAIRMAN. Professor Baxter, let me follow up a minute on my question about the patents. Don't you think there should be mandatory licensing of patents developed in the past with regulated funds as well as those patents which would be obtained in the next several years based on past research?

Mr. BAXTER. There is a transitional problem there, to be sure. In our view any patents that have already been obtained will become subject—are subject—to the mandatory licensing requirement. That is as it should be.

It seemed to us that a simple cut at the time the decree, the modification, became effective was the best way to handle that

problem. It would not be unreasonable to go further and say, well, all the patents you get within 1 year or all the patents you get within 2 years—basically you are constructing some sort of presumption that the patents that come out over some time horizon were really financed with the old source of funds, but I don't know what the right time horizon would be. I am sure that you create incentives on the part of the company to try to gain from the system and to delay an application's filing.

I really think that, since any time period you seize upon there would have very arbitrary features, the simplest and cleanest, and therefore I think the best way is to say as of the moment the decree is entered, subject to mandatory licensing before and not subject after.

The CHAIRMAN. Professor Baxter, under the terms of the proposed modification, the BOC's may create a shared organization for provision of certain centralized services. Would it concern you if such an organization were created to facilitate procurement?

Mr. BAXTER. No, it would not. In some ways that is the same question about whether I would be concerned if there were only one BOC. I would think that in some instances the BOC's affiliated through that jointly held enterprise would almost certainly wish to use it for procurement. As I have indicated, I do not see that as a significant problem.

The CHAIRMAN. Professor Baxter, under the proposed modification is AT&T permitted to share multifunction facilities with the BOC's? If so, does this anticipate new construction with multifunction capability, so that such sharing arrangements could continue indefinitely?

Mr. BAXTER. Multiple ownership or joint ownership is not permitted by the decree, but joint usage is permitted under tariff provisions. Indeed, there is a sense, of course, in which the entire local network is used by the long lines carriers for the purposes of message termination or origination.

The CHAIRMAN. Professor Baxter, should AT&T be permitted to buy its entire equipment requirements from Western Electric?

Mr. BAXTER. Should AT&T be permitted to? Now after the divestiture, of course, AT&T will be a competitive company that includes Western Electric among its affiliates. It should be permitted to buy its equipment anywhere it wishes to buy its equipment. After the separation, the operating companies will be independent of AT&T. They, too, should be permitted to buy their equipment wherever they can find best quality and lowest price. At that point they will have no affiliation and, therefore, no incentive to favor AT&T. I would say, yes, they, too, should be permitted but not required, of course, to buy all their equipment from Western Electric if that is where they can get the best deal.

The CHAIRMAN. Professor Baxter, do you think there is a legitimate concern that retention of customer premises equipment by AT&T will give it a significant advantage over competing equipment manufacturers by providing it with detailed customer information?

Mr. BAXTER. I am not sure I understand the full import of that question. The provision of customer premises equipment is obviously a function which is potentially competitive and should occur in a

competitive arena. The AT&T company will have a large inventory of equipment. That is not necessarily an advantage. I do not see any particular sense in which AT&T would have a significant advantage over other carriers, other vendors of CPE.

The CHAIRMAN. What about information they would gain about customers' practices?

Mr. BAXTER. Of individual customers' practices—that this particular household likes one white phone and one brown one or that this business——

The CHAIRMAN. Primarily business equipment.

Mr. BAXTER. Business equipment. Yes; they will know what is installed, but it is not hard for a competitor to find out what is installed. Of course, no one knows whether what is installed is optimally suitable at the present point in time. I just see no reason why that market should not function in an intensely competitive way. Indeed, I think it is already functioning quite competitively. There are a number of vendors of equipment of that sort.

The CHAIRMAN. Professor Baxter, do you anticipate the possibility that one or more of the BOC's could be acquired by either foreign entities or companies that have not previously been involved in telecommunications, and do you think such a result would be good or bad?

Mr. BAXTER. No; I would not welcome that result at all. I would view it with some alarm. Indeed, the entire premise of what we have done here is that a regulated enterprise that has available to it a natural monopoly position such that they would be able to make very, very significant profits by raising their prices but for regulation—that it is very dangerous to let such an enterprise combine with enterprises of other types because, to the extent that the costs of the affiliated enterprise can in any way be smuggled across that boundary line and masquerade as costs of the regulated enterprise, then the regulator permits price to rise in the regulated market and you have this engine of cross-subsidization there.

The phenomenon that you suggest would simply recreate the problem that we have been attempting to solve in this case in a different context, this time with a foreign enterprise in accordance with your hypothetical. I would regard that with some displeasure.

The CHAIRMAN. Professor Baxter, do you believe that the interest of the BOC's can be adequately represented even though they have no independent counsel in this matter?

Mr. BAXTER. Yes; I do. One must remember that AT&T has shareholders. AT&T is going to package the BOC's into some number of boxes—it is not important for present purposes what that number is—and is going to distribute to its shareholders shares in those packages. AT&T has a fiduciary obligation to its shareholders regarding the value of the set of shares that the shareholder winds up holding—shares in AT&T, shares in operating companies 1, 2, 3, and 4—they will hold all those pieces of paper on the day divestiture occurs.

AT&T has a fiduciary obligation to maximize the value of those shares in the hands of their shareholders. If they engaged in some, what I would regard as, self-defeating game of creating operating companies with no assets or some other nonviable form of enterprise, they would not fulfill that fiduciary obligation. There will be

plenty of lawyers looking for potential class actions on the part of AT&T shareholders. I regard both the shareholders and, derivatively, the operating companies as already being very well represented.

The CHAIRMAN. Professor Baxter, although eventually the BOC's have to provide exchange access to all interexchange carriers through a uniform number of digits, wouldn't it be preferable to specify a time limit on how long this should take?

Mr. BAXTER. I was not prepared to specify or try to fight for a time limit in the modification. If the Congress wishes to specify a time limit, certainly I would see nothing wrong with that. I do not know how long the time limit should be. The conversion will require a significant reprograming of switches at the local operating company level, both AT&T companies and the other companies. It will be quite expensive.

I am not sure what the limit should be. Therefore, I did not try to get one into the modification. It simply essentially is silent on that point, although it acknowledges that is a problem.

The CHAIRMAN. Professor Baxter, under the modification, differences in exchange access charges to carriers must be cost justified. Do you think it would be desirable to also reflect any decreased value to a carrier who is unable to obtain equal interconnection?

Mr. BAXTER. The decree is very clear that the local operating companies are not precluded from affording less than equal services at lower costs to the extent they wish to do that.

After the separation occurs, after the BOC's are no longer affiliated with the surviving AT&T company, they should have every incentive to afford a lesser quality of service to some long distance carriers or information providers, if that is what that carrier or provider wishes.

There is an interim problem there. At the present time, as you probably know, under FCC regulations AT&T is required to provide less than equal service at reduced prices essentially. The decree does not tell the FCC to stop doing that. The FCC is free to go on handling the problem in that way. That in my view was an adequate way of coping with the transitional problem.

The CHAIRMAN. Professor Baxter, it would appear that Glass 4 toll offices will be placed with AT&T after the divestiture of the BOC's. Do you have any concerns that this will create significant difficulties for equal interconnections?

Mr. BAXTER. It does create difficulties for equal interconnection. One has to draw a line somewhere and say local service stops here and long-distance service starts at the same point. That was the best place we could find to draw the line. The other long-distance carriers are going to have to provide switches that perform the routing functions that the AT&T class 4 switch provides today. The decree requires that the BOC's get the signals to them, to their class 4 switches, which still have to be brought into existence by and large at a cost that does not exceed the cost to AT&T of getting the signals to its class 4 switches.

One could have solved the problem in a variety of slightly different ways, but they all posed problems of one kind or another. That is the way we chose to solve it. However, you are quite right; that was one of the most difficult and sensitive features of the negotiations and, indeed, of our own analysis.

The CHAIRMAN. Professor Baxter, is it anticipated that the Justice Department would have sole enforcement authority over the terms of the plan of modification or would this authority be shared with the FCC?

Mr. BAXTER. There are two quite different kinds of authority there. The FCC derives its authority from the terms of the 1934 Communications Act. That authority is in no way diminished by the court order entering this decree, if it should be entered as a decree.

On the other hand, we have authority from the antitrust laws to enforce the antitrust laws and from the court order to do what this decree says we may do. The two authorities would coexist. We, of course, would consult with the FCC and seek their expert judgment on a variety of matters in the process of implementing this modification, but the two sources of authority are really quite independent of each other.

The CHAIRMAN. Professor Baxter, how and by whom is it anticipated that assets involved in the divestiture will be valued?

Mr. BAXTER. Of course, the regulatory commission with regulatory authority will decide the magnitude of the rate base of the enterprise over which it has authority. If some assets are distributed away from the basic operating companies to the surviving AT&T company, I would suppose that the local public utility commission would want to reduce the rate base accordingly. In that context, it would be the local PUC that was doing the evaluating, subject of course to judicial review and constitutional protections of various kinds.

The only place where that problem really arises is the problem of defining and quantifying the regulatory rate base.

The CHAIRMAN. Professor Baxter, what impact, if any, do you believe that the proposed modification should have on the FCC in the Computer II settlement decision?

Mr. BAXTER. I would say the decree has no direct effect on the FCC. Its statutory authority is derived from the Communications Act. The decree does change the world; there is no doubt about that. It changes the characteristics of the industry. I would suppose that the FCC would wish to take another look at its decision in *Computer II* and see whether it thinks that decision is still the optimum order that can be entered in view of the now-changed characteristics of the industry, but that of course is entirely a decision for the FCC.

The CHAIRMAN. Professor Baxter, would you recommend that Congress continue with legislation to supplement the consent agreement to deal with problems such as rising telephone rates and the various other competitive issues which we have been discussing here today?

Mr. BAXTER. I am reluctant to make recommendations to the Congress. Certainly, I have no authorization from the administration to do so. We have not ourselves really finished the project, although we have undertaken it, attempting to sketch out the legislative responses that the Antitrust Division would think optimum in view of the changes that will occur in the industry.

My guess is that the Congress probably will want to pass some legislation but, as I think I suggested to Senator Hatch a few mo-

ments ago, I would think it probably was a good idea to let a little more dust settle, to take a look at what this plan of reorganization looks like, before serious efforts in that direction were made.

The CHAIRMAN. Professor Baxter, I have a few more questions, but we will ask that you answer those for the record in order to save time.

Mr. BAXTER. Yes; certainly, Mr. Chairman.[1]

The CHAIRMAN. Turning to the dismissal of the *IBM* case, I have a question. Professor Baxter, there have been reports to the effect that your decision to dismiss the *IBM* case was contrary to the recommendation of the trial staff. Is this true? If so, what were the significant differences between you and your staff?

Mr. BAXTER. The trial staff as an entity did not make any recommendations to me. Certainly, it is true that my decision in the *IBM* case was not agreed to and I am sure would be disapproved by particular members of the trial staff. I hesitate to attribute any particular view to any particular individual, but I am very, very clear that there were members of the trial staff who did not approve of what I was doing; indeed, strongly disapproved.

However, it was not their decision to make. I made it after a great deal of careful study and soul searching.

How do I account for the fact that they viewed matters differently? I guess I would say only this: I have done some litigating in my professional career. It is my experience that when one is involved in litigation for a period of time, one acquires a kind of commitment that the world is the way you are trying to make it appear in the litigation. I have never encountered a litigator who thought he was losing a case right up until the last second before the judge hands him his head in a basket. Litigators expect that they are winning or will win.

I think all these things affected the trial staff and its judgment. I do not mean to suggest that they were blind in any respect, but just that when one has spent 13 years on a project one finds it very, very difficult to accept the proposition.* * *

Senator METZENBAUM. Mr. Chairman, I wonder if this committee could receive a copy of the staff memoranda with respect to their recommendation concerning their position against dismissing the case?

Mr. BAXTER. I am sorry, but I forgot exactly where I was on that sentence.

The CHAIRMAN. I did not hear you.

Mr. BAXTER. I said I forgot exactly where I was in the sentence.

The CHAIRMAN. He is asking if you could furnish a copy of the staff memorandum. Would you object to doing that?

Mr. BAXTER. Yes, I would, Mr. Chairman. Internal documents written by career people for advice within the Department should be written by them without concern as to how they will be viewed when and if they should ever become public documents. I regard them as confidential documents.

Senator METZENBAUM. Would you be willing to furnish them without identification of the author?

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[1] Can be found on page 122.

I think it is important in our oversight responsibilities that we know exactly what the staff's thinking was in that you then came to a contrary conclusion.

Mr. BAXTER. That is an understandable position. I had not considered that as an intermediate step. May I think about that one, Senator Metzenbaum?

Senator METZENBAUM. Will you advise the chairman——

Mr. BAXTER. I will.

The CHAIRMAN. If you will think about that and if you could explain their position and why you took a different position, if you could do that for the record, we would like to have that.

Mr. BAXTER. I can tell you what their position was if you would like to ask me to do so.

The CHAIRMAN. I have been asking questions for about 50 minutes. I am going to turn over the questioning now to the distinguished Senator from Ohio. He can take an hour if he wants to do so. After that is finished, we will proceed to the AT&T witnesses unless it is lunchtime. After Senator Metzenbaum finishes, Senator Specter has the right to ask questions, too. Then it probably will be time to recess for lunch. The AT&T witnesses could start at 2:30.

Senator Specter, would you take the Chair now, please?

Senator Specter may recess for lunch at a reasonable time. I suggest 2:30 but, if he wishes to revise that, he may feel free to do so.

We will recess for 10 minutes at this time.

[Recess taken.]

Senator SPECTER [acting chairman]. The committee will come to order. The questioning will be resumed by Senator Metzenbaum of Ohio.

Senator METZENBAUM. Mr. Baxter, Senator Thurmond asked you a question about the impact on the consumer, and you indicated that you did not feel that there would be any impact upon the consumer because of this flow of funds back and forth. Now that concerns me because every single published report on this subject has indicated that the consumer will indeed be affected. The New York Times story was "Local Rate Rise Viewed as Likely. End of Long Distance Subsidy Expected to Spur Increase."

It went on to say: "The long distance subsidy will be gone and obviously the local companies will be under a lot of pressure to raise prices, said J. Grossman, a spokesman for AT&T." You have The New York Times and you have AT&T itself saying the rates are going to rise. Then in the balance of the story it indicates that, "Most analysts said that while local service charges would jump substantially, long distance charges would decline."

In addition to that, we are aware of the fact that the House subcommittee indicated that the settlement will result in a loss of $12.6 billion in annual local service revenues to the new local companies.

Under that kind of published information and the statement of AT&T, as well as the statement of the analysts, would you be good enough to explain how you alone, of all people in the country, seem to be saying that local increases are not to be expected?

Mr. BAXTER. I have never thought things of this sort should be decided——

Senator METZENBAUM. I am sorry, but I cannot hear you.

Mr. BAXTER. It has never been my view that questions of this sort should be decided by a majority vote. I cannot help what the press has been writing about this. It rests on a misunderstanding.

What underlies those statements is an implicit assumption that the present division that occurs in the separations process, the allocation of cost of so-called non-traffic-sensitive plants, will be eliminated and that the revenues that are presently brought to the local companies by the separations process will come to an end. That simply has no basis in fact or law.

The exchange access tariff that I have described is susceptible to carrying precisely the same dollar flows, to the penny, back to the local companies if the regulators choose to use them that way.

Now, what I said was that the decree will have no effect on the relative cost of local and long distance service, and that is correct.

It is a quite different question to ask whether in the future local rates will go up. I think most analysts expect local rates to go up. Certainly they will go up in dollar terms as a consequence of inflation. Local telephone service is no longer, it seems, subject to the rapid technological changes that permit dollar costs to fall even in the face of some level of inflation. I do not doubt that local calls will go up, but they will not go up because of the decree. The decree creates a vehicle for cross-subsidization to take the place of the present vehicle. Now, if the regulators do not choose to use it for that purpose, that is a different matter but the vehicle is there.

Senator METZENBAUM. If you take away some of the cream of the telephone business, such as yellow pages and other aspects—and we will get back into this question of the yellow pages in a minute—then do you not leave the local companies with that $12.6 billion loss of revenue? Is not the only alternative that they have to seek higher rates in order to make up that $12.6 billion?

Mr. BAXTER. No, it is not. They can recover them through the exchange access tariff.

Senator METZENBAUM. But if the access charges are too high, is it not a fact that the big users will go off line and thereby bypass the local companies? If that happens, then rates to consumers would go up even more, wouldn't they?

Mr. BAXTER. If the exchange access tariff is set so as to achieve the present level of subsidy, assuming there is a present level of subsidy, then there will be precisely the same incentive to bypass that there is at the present time.

Senator METZENBAUM. Professor Baxter, you have indicated in very strong language, unequivocal language, that the yellow page revenue will remain with the local companies. Did I understand you correctly on that?

Mr. BAXTER. That is not exactly what I said, but it is a reasonable approximation of what I said.

Senator METZENBAUM. OK.

Mr. BAXTER. The yellow page revenues I think of as being susceptible to disaggregation into two components. There are certain real costs associated with producing the yellow pages. Obviously, it is consumptive of paper and ink. One has to seek display advertising, solicit display advertising. One has to transport the yellow pages from the printer to the people who wish to have a copy of the

yellow pages. Those are all real costs. Of course, the revenue stream is sufficient to cover those costs.

Senator METZENBAUM. That is an extremely profitable end of the business, isn't it?

Mr. BAXTER. The part of it that I have been talking about so far is not where the profit lies. The profit lies in the fact that they have been able to maintain prices for the yellow pages well above costs, which I just finished describing.

One must ask, why isn't the price of the yellow pages driven down, as it would be by competition, to its costs, so that it is not extremely profitable for anybody? Competitive activities are not extremely profitable; they just return competitive rates of return.

The answer is that there is a very, very important feature of monopoly power in the yellow pages. What gives rise to the monopoly profits that are associated with the yellow pages is the monopoly which the local telephone company has over the computerized listing of local business phone numbers. That computerized listing is something that the local companies will be in a position to sell off.

Although somebody else may be performing the physical task of soliciting display advertising, printing, and distributing the books, they will be doing so under competitive conditions only after some winning bidder has succeeded in paying over to the local operating company the monopoly profit that is associated with the exclusive listing of the local phone numbers.

Senator METZENBAUM. That exclusive listing, is that a regulated rate that they will sell it for or is that an unregulated rate?

Mr. BAXTER. The local public utility commission can handle that however it wishes. One way to do it would be to let the local telephone company sell it for the highest attainable price and make all that revenue into regulated revenues and reduce other rates downward in view of that revenue stream.

Senator METZENBAUM. Mr. Baxter, in view of what you have just testified to, how do you explain the inconsistency in section II(d) which provides that, "No BOC shall directly or through any affiliated enterprise" do one of several things. The third one is "provide any other product or service except exchange telecommunications and exchange access service that is not a natural monopoly service actually regulated by tariff."

If each company is so limited, then my question to you is this: Again, you seem to be the one individual in the country who interprets the fact that the local companies will be able to obtain yellow page revenue when everybody else who has interpreted this has come to a contrary conclusion. Let me read you something from the Wall Street Journal.

"The split as currently envisioned would result in the local telephone companies keeping the more than 1 million public telephone booths around the country. Dial-a-services such as dial-a-joke aren't considered regulated telephone business, and so would go to AT&T. So would the extremely profitable printed yellow pages business; white page directories, money losers, would go to the local telephone companies because such listings are considered part of basic telephone services."

In addition to that, the committee of the House that has been handling this matter was reported in the Washington Post as

having stated, "The drop in revenues comes from the loss to local companies of long distance facilities, customer equipment, and the yellow pages, revenues which will instead be in the hands of the remaining AT&T."

You have now said in the first instance that there will not be any rate increases to the consumers as a result of the settlement. Now you are saying that the revenues, the really profitable aspect of the revenues which could be sold off to the highest bidder, would be part of the local company's revenues. The Wall Street Journal comes to a contrary conclusion. Every analyst that I have read about has come to a contrary conclusion. The language of the settlement agreement would lead one to the same kind of conclusion.

My inquiry of you is this: How did you come to your conclusion that the local BOC's would be able to sell these lists to the highest bidder?

Mr. BAXTER. As for the language, I wrote it. I really do not know what to say. I cannot take responsibility for the fact that many of the newspapers have talked to analysts who did not get things right.

Senator METZENBAUM. Is the yellow pages income a part of regulated income? You, yourself, just said publicly that they could auction it off to the highest bidder instead of regulating. Therefore, if they could do that, it is obviously unregulated. Therefore, if it is unregulated, it is not within the limitations of section II(d).

Mr. BAXTER. If the local public utility commission requires them to conduct an auction of the exclusive rights to publish the yellow pages and takes the revenue in as regulated revenues in computing other rates, it satisfies the requirements of the paragraph that you have just read. I would expect that is what they would do.

Senator METZENBAUM. But that is if the local PUC requires that. The fact is that if AT&T makes arrangements with those that it leaves in charge of the companies—and, as you indicated in your statement, there will be a kind of institutional loyalty of the former executives of AT&T who are operating the local companies to the parent company—then the parent company is going to get these revenues; the local company is not going to get these revenues.

The question I have is: How do you come to the conclusion—where is there anything stated in the settlement language which would provide that the local companies would get that yellow page revenue?

Mr. BAXTER. The property right that is represented by the exclusive possession of that computerized listing is inherently in the hands of the local companies. If the local companies during the transition period were, for reasons of what you have termed "parochial loyalty," to attempt to give that property away to the affiliated parent, it would be the job of the public utility commission to stop them from doing so, just as it should stop them from giving away any other right.

After the separation, of course, one would be left totally without explanation for why they should transfer this property right of enormous value to an unaffiliated company. In either event, the public utility commission should require that those revenues be captured for the local basic operating company. The decree in

many respects does not tell the local public utility commissions how to do their job, but I suspect they will do it adequately, nevertheless.

Senator METZENBAUM. Mr. Baxter, has the question of yellow page revenue been discussed by you with the representatives of AT&T during the settlement negotiations?

Mr. BAXTER. Yes.

Senator METZENBAUM. Do they agree with your interpretation that the local companies will be able to receive the funds that will be available by reason of the selling of the lists?

Mr. BAXTER. I understand that they do, but they are here to speak for themselves.

Senator METZENBAUM. Under those circumstances and in view of the misinterpretation that has occurred throughout the country in the media as well as by a congressional committee, do you think it feasible to expect that you and they might agree to a supplemental item to be included in the settlement agreement to this effect?

Mr. BAXTER. I think the explanation should be sufficient, but I would have no way of answering that question for them. I would not have any particular resistance to that beyond the procedural complexities it would involve.

Senator METZENBAUM. It would not be too complex to add a sentence or to put something into this very paragraph indicating that the local companies would be entitled to receive those funds which would be flowing from the publication from the yellow pages, or at least the sale of the list in connection therewith.

Mr. BAXTER. The sale of the listing, I quite agree. However, the important distinction to keep in mind is between the sale of the local machine-readable listing and the physical function of publishing and distributing the yellow pages.

Senator METZENBAUM. Do you think that the parent company or the local companies would be precluded from awarding the right to publish the yellow pages and being selected on an exclusive basis for those lists under this decree?

Mr. BAXTER. I am afraid I did not follow the question, Senator.

Senator METZENBAUM. Under this decree do you think that the local companies would be precluded from awarding on an exclusive basis the lists that you have just described as being that most valuable asset?

Mr. BAXTER. There is nothing in the decree that would keep them from awarding on an exclusive basis, and I would think it would be foolish for them to do anything else.

Senator METZENBAUM. Foolish for them to do anything else? I am not sure——

Mr. BAXTER. Anything other than auction it off in substance on an exclusive basis, because that is what will maximize their revenues.

Senator METZENBAUM. But my question is this: Is there anything in the decree—I think you and I came to a different conclusion on the exclusive basis. I am not questioning the fact that the local companies, according to you, would have the right to put it out on an exclusive basis. Query: Would the local companies under the decree be permitted to put it out on an exclusive basis and award the contract without competitive bidding to AT&T?

Mr. BAXTER. There is nothing in the decree that would keep them from doing that, but I would regard it as a violation of their obligations to their own shareholders and to the local ratepayers.

Senator METZENBAUM. Could we assume that before this matter is disposed of before Judge Greene that you might explore this subject with AT&T in order to see whether or not clarifying language could be included in the settlement agreement?

Mr. BAXTER. I certainly will be more than happy to talk to the representatives of AT&T about the problem.

Senator METZENBAUM. Would you address yourself to the impact on AT&T's employees and whether or not that subject has been discussed in connection with the settlement negotiations? What agreements or understandings have been arrived at with AT&T on that subject?

Mr. BAXTER. After the divestiture there will be two, three, four, or five companies representing the present totality of AT&T's assets and functions. I have no reason to think that the number of employees who will be needed to perform those services will be either more or less than the present number. I do not see that there should be any significant effect upon the employees at all, although some may wind up working for one company when they would rather have been working for another, or conversely.

In any plan of divestiture of the kind that is contemplated by the decree, there will undoubtedly be provisions pertaining to pension rights and security matters. That is to be expected.

As to your other question: Was there any discussion of these matters? No, not explicitly. I certainly contemplated—and I assume, but only assume, that the company representatives contemplated—that provision would be made with respect to these matters in the plan of divestiture which is required 6 months after the entry of the modification.

Senator METZENBAUM. So the whole question of pension rates and the kind of pension that will be established by the new companies, and the fact that S. 898 includes elaborate employee protective provisions, none of these subjects actually were explored at the time of the settlement negotiations?

Mr. BAXTER. That is correct.

Senator METZENBAUM. What consideration have you given in this matter to the impact on AT&T's competitors? Was that discussed? What is your view as to what the impact will be on competitors?

Mr. BAXTER. That was discussed very extensively. Of course, the impact on consumers, which is in significant part derivative from the impact on competitors, has been my central concern and is the central antitrust concern with the entire case.

Now there are a variety of different competitors that one must take into account, and the impacts differ competitor-type by competitor-type.

For example, there are competitive and potentially competitive manufacturers of switches and wire and other telecommunications apparatus of various sorts. Our concern heretofore, and one of the concerns underlying the antitrust complaint itself, was that they were not being afforded an equal opportunity to sell that equipment to the local operating companies. Their position should be significantly improved. In the short run, it should be improved by the

requirements for nondiscriminatory treatment. In the long run, it should be improved by the dissolution of the affiliation between the AT&T company and its Western Electric subsidiary on the one hand and the local operating companies on the other hand.

Senator METZENBAUM. I think your answer assumes that there will be a number of companies. Am I to read into that answer the implication that the Department of Justice, the Antitrust Division, would oppose a spinoff which would result in one national holding company of the 22 separate BOC's?

Mr. BAXTER. I really have not addressed that. I do not expect that the AT&T company will find a single national BOC an attractive way to go. However, the mere fact, if it were to become a fact, that there was only one basic operating company by no means suggests that they would be likely to buy all of their equipment from a single source. There are many large companies that make multisource equipment purchases. Indeed, it is regarded as very bad business practice not to multisource in most industries with which I am familiar. I do not regard that as a realistic prospect.

Senator METZENBAUM. Apparently you would then challenge this statement that was carried in the Wall Street Journal by a man whom I do not know but apparently, is a recognized authority in the field. Mr. Lee L. Selwyn, president of Economics and Technology, Inc., a Boston consulting firm specializing in telecommunications regulation, is concerned about the option of a single national holding company.

"If they choose to go with that," he says, "then we wind up with one giant seller of telecommunications equipment and one giant purchaser. That creates an absolutely open invitation to collusive behavior between AT&T and its former local service subsidiaries," he added.

You would not agree with Mr. Selwyn in that?

Mr. BAXTER. No, I would not agree.

Senator METZENBAUM. On page 5 of your testimony, you indicate that the divested operating companies may retain "some institutional loyalty." What steps will be taken during the more than 18 months AT&T will be in control in order to see to it that AT&T does not insure the loyalty of the operating companies by placing its people in all of the high administrative positions of the operating companies?

What I am saying is this: In this period, the company certainly is aware of the fact that some people presently operating local companies are probably closer tied in with the parent company than are others. During this 18-month period, the company has the right to change such personnel as it desires to change. There is no limitation on that.

What assurances, what protections, will be provided to see to it that this very matter of institutional loyalty about which you speak in your submitted statement will not work to the disadvantage of the competitive market and the consumers of the country?

Mr. BAXTER. As I indicated, although we rely primarily on the fact of separation after 18 months to prevent this sort of behavior, we wrote in provisions which require equal treatment of vendors of equipment, equal treatment of interconnecting long distance carriers, in an attempt to address the interim 18-month problem.

Enforcement difficulties with respect to such injunctive-type relief are always difficult. I am not sure that it will redress the problem 100 percent, but it should make a good start on it.

This is a problem that has been with us since shortly after the turn of the century. The next 18 months will represent perhaps 2 percent of the time period during which that problem has been with us. If we have arrived at a satisfactory resolution of that problem at the end of the 18-month period, then although I regret that we were not able to do better with it during the next 18 months, I guess I do not regard that as a serious shortcoming, either.

Senator METZENBAUM. Under the settlement, Mr. Baxter, who has responsibility for evaluating AT&T's plan for splitting up its long lines and local business?

Mr. BAXTER. For evaluating their plans?

Senator METZENBAUM. Its plan, yes. AT&T has to come up with a plan. Who is going to make an evaluation of that?

Mr. BAXTER. The decree provides that we will make the evaluation of that.

Senator METZENBAUM. Do you anticipate any judicial review of the divestiture plan assuming the settlement itself is approved?

Mr. BAXTER. Of course, anyone can always go to court. Certainly we can go to court, AT&T can go to court, or others can go to court and ask for a modification of the decree that would contradict some feature of the plan if it were thought not to be satisfactory.

Senator METZENBAUM. Mr. Baxter, you said anybody could go to court?

Mr. BAXTER. Well, not literally anyone. They would have to petition to intervene in some respect.

Senator METZENBAUM. Who could intervene? Would the Justice Department react negatively if some consumer-oriented group attempted to file a brief amicus curiae or filed a motion to intervene in connection with the settlement or the divestiture agreement?

Mr. BAXTER. Or the divestiture? It would depend entirely on the position they were taking and whether or not we thought it was sound.

Senator METZENBAUM. Would it be fair to say that the Justice Department would welcome some consumer involvement in attempting to protect the consumer or public position and would not just summarily indicate its opposition to their intervention?

Mr. BAXTER. That is a really terribly vague question. I am not sure of the form in which that would come. We certainly would welcome the filing of amicus presentations of the kind you have in mind.

Senator METZENBAUM. I understand that. Without being vague, what I am really saying is that in connection with the divestiture agreement, assume that groups such as the Consumer Federation of America, one of Mr. Nader's operations, or X, Y, or Z responsible, reputable organization—perhaps the Small Business Association of America, perhaps the National Federation of Independent Businesses, or the Business Roundtable—if any of them wanted to intervene, not just to file a brief amicus curiae, is it fair to say that the Justice Department would or would not object to their intervention?

Mr. BAXTER. I expect that we would oppose intervention petitions generally.

Senator METZENBAUM. So, the only way that the American people can be protected is if the Department of Justice, Antitrust Division, and AT&T would see fit to protect their interests. Absent some special ruling by Judge Greene, there will be no court approval of the divestiture agreement, will there?

Mr. BAXTER. We have two different processes that seem to me to be getting confused, or perhaps it is only I who am confusing them.

There will be hearings on the proposed modification, this piece of paper that we have before us. I would expect, out of a concern that if intervention were permitted there might be scores of intervening parties and we might be tied up there in that courtroom for the next 3 years, that the Division would in general oppose intervention proceedings applications in those hearings.

At the very same time, the purpose of the hearings and the process contemplated by the Tunney Act is for people to be able to make filings and express their views, whatever they may be. We certainly contemplate and welcome that.

Presumably when those hearings are over if the judge decides that the proposed modification is in the public interest, he will approve its entry as a decree. Not more than 6 months thereafter, the company has an obligation to file a proposed plan of reorganization. The decree provides that is submitted to the Department of Justice for approval.

Again, we will undoubtedly solicit advice from a number of sources and would be receptive to receiving advice from any source, but no formal hearings are contemplated at that particular point in time.

It is not entirely certain to me which of those two processes you are asking about or the precise procedural vehicle that you are talking about.

Senator METZENBAUM. What I am particularly concerned about is not the modification, because that is in the hands of Judge Greene and I can understand that. The question I am concerned about is the divestiture plan and whether or not, as I understand it at this moment, absent Judge Greene's requiring a modification of the settlement agreement, he would not even have the right to look at that, to supervise it, to criticize it, and to require changes.

My question then is: Will the Justice Department welcome Judge Greene's having continued jurisdiction with respect to the divestiture plan?

Mr. BAXTER. The judge will in due course have continuing jurisdiction. Indeed, the decree provides for the continuing jurisdiction of the judge.

Senator METZENBAUM. So the divestiture plan will not be a document just approved by the Justice Department but, as you see it, it will have to be submitted to Judge Greene for approval?

Mr. BAXTER. No. The modification calls for the submission of a plan of reorganization to the Department of Justice. Now that can be brought before the judge as in the exercise of his continuing jurisdiction, but someone would have to take steps to bring it before the judge. It would not come before the judge under the terms of the proposed modification.

Senator METZENBAUM. Can the judge at this stage of the proceedings, while he presently has jurisdiction of the matter, require the divestiture plan to be submitted to him before the matter finally is disposed of?

Mr. BAXTER. I think as a technical matter he could not do that because that would amount to his modifying the parties, agreed proposed modification. He can reject the modification as not being in the public interest. He can accept it. However, he has no general power to modify.

Senator METZENBAUM. He can accept it conditioned upon his continued jurisdiction.

Mr. BAXTER. Yes.

Senator METZENBAUM. That would be one way he could achieve his objective, isn't it?

Mr. BAXTER. I think it is.

Senator METZENBAUM. I hope he gets the message.

Are there any restrictions on the manner in which AT&T can enter the enhanced services markets? Could they buy up IBM? Could they make major acquisitions? Could they just move out and become a monolithic and dominant factor in the enhanced services market by a series of acquisitions?

Mr. BAXTER. Of course they, remain subject to a wide variety of State and Federal laws that would impose some checks on their ability to do any of those things, but, in general, they become an unregulated, competitive enterprise and are free to enter the enhanced service business in such ways as seems appropriate to them.

Senator METZENBAUM. Mr. Baxter, in your first news conference as Assistant Attorney General you said that:

> Any settlement of the AT&T case should separate all the regulated companies of the enterprise from the unregulated components. Otherwise the company would have a license to print money through cross-subsidization from the regulated components.

This settlement really does not accomplish that goal, does it? Long Lines would still remain regulated.

Mr. BAXTER. If you take it literally, you are quite right that it does not accomplish that. I already explained this morning that the Long Lines activity, although it is a regulated activity and literally within the language I used that day, does not enjoy statutory entry barriers, is rapidly becoming more competitive, is accelerated in the rate at which it will become competitive by other provisions of the decree, and therefore does not represent a very substantial source for the purposes of cross-subsidization.

I do not think it is a significant shortcoming of the relief we obtained in the case that only the basic operating companies as opposed to the Long Lines Division are separated. However, if one takes the general language I used last April literally, then it is true that the decree does not precisely correspond with that language.

Senator METZENBAUM. As you know from your academic days, there have been a good number of treatises written on antitrust law. One is by Areeda and Turner. They discuss section 2 Sherman Act violations in the following manner. My question in this respect has to do more with IBM and the dismissal of the *IBM* case.

We are concerned with exclusionary behavior, that which prevents actual or potential rivals from competing or which impairs their opportunities to do so. Exclusionary behavior should be taken to mean conduct other than competition on the merits or other than restraints reasonably necessary to competition on the merits that reasonably appear capable of making a significant contribution to creating or maintaining monopoly power.

Why is this description of impermissible exclusionary behavior not applicable to IBM's conduct, especially with respect to Control Data?

Mr. BAXTER. With respect to what?

Senator METZENBAUM. Control Data.

Mr. BAXTER. You mean Control Data Corp.?

Senator METZENBAUM. Yes.

Mr. BAXTER. Are you talking about the 360/90 episode?

Senator METZENBAUM. I am.

Mr. BAXTER. I thought I had gone into that at some length, but I would be happy to do so at such greater length as you wish.

I said that that could be seen as an episode of predatory behavior, but the difficulty was that Control Data was not a participant in the market that the Government alleged IBM had monopolized. Control Data Corp. has never made machines—at least it has never had any significant machine—in the market of large computer systems optimized for business use. Control Data's machines, to the extent they are significant, are important competitors in the large scientific market.

If the 360/90 episode is to be viewed as an effort of predation; (a) it was in a market that was different than the market alleged to be monopolized; (b) it was aimed at a competitor who was not a competitor in the relevant market; and, (c) it was totally ineffectual in the sense that CDC sold far more machines by more than an order of magnitude than IBM did.

Senator METZENBAUM. Did IBM's actions not discourage Control Data from entering IBM's general computer market? Was that not the problem, that although it was not directly competitive, it was a means of sending a message to Control Data?

Mr. BAXTER. That was the theory, but there was never any clear evidence that Control Data had contemplated entering the business machine market. It never did enter the business machine market. It is difficult to conclude that its ability to enter the business machine market, if it wished to do so, had been significantly lessened by the 360/90 episode.

Senator METZENBAUM. Mr. Baxter, do you think a Government official is ever justified in changing the Government's course of action whether it is in a criminal proceeding, a civil proceeding, or in any kind of activity merely on the basis that so much time has elapsed? For example, the prosecutor in the criminal case might just say, "I am weary of this case. I have been up and down to the courts for years. I have been reversed. We have had to retry the matter. I think I have just had enough of this case." Or in the case of IBM to say, "I think I have had enough of this case and I think it is time to call a halt."

Should that ever be part of a Government official is consideration in making a determination to proceed forward or to bring a halt to the proceeding?

Mr. BAXTER. In general, I would say no. Certainly it would be unacceptable to take the view that one should not bring or persist in a case merely because it was going to be a long, difficult, and expensive process. That would send a very unfortunate signal that, if a large company can make the process sufficiently long and sufficiently expensive, they would acquire a kind of immunity. That simply would not be an acceptable point of view. Certainly the *IBM* case was not disposed of simply for those reasons.

Senator METZENBAUM. Thank you, Mr. Baxter.

I will expect further response with respect to the memorandum that Senator Thurmond asked about without having any attribution as to who the authors are.

Mr. BAXTER. We will attend to that, Senator.

Senator METZENBAUM. Thank you.

Senator SPECTER. Professor Baxter, as we convene the second session of the 97th Congress, I think it appropriate to note what a busy year the Justice Department has had in its Antitrust Division. I note in your statement the comment about these matters being the two most important which you have handled. Preliminarily, I would want to congratulate you on your work in the past year. Notwithstanding that there may be some differences in judgments, it has been a very active year for you and I think a very good one.

Mr. BAXTER. Thank you, Senator.

Senator SPECTER. You have testified about the very significant change on fund flows which will be occasioned by the settlement decree. There have been extensive questions already propounded about the possibility that rates to the consumers could go up by as much as double. You have been very candid in saying that you cannot offer any assurances that that will or will not happen because it depends on a great many factors.

Since it is a distinct possibility that rates to telephone users could double, might it not be in the best interests of the American consumer who uses telephones to have this settlement proposal rejected and to leave AT&T in charge of the local operating companies?

Mr. BAXTER. I should think not. In the first place, as I have explained several times, whatever happens to local rates will not be because of anything in the decree. I do not know any sense in which leaving things in the hands of AT&T would represent an improvement.

The thought may be that AT&T would have the wherewithal to engage in cross-subsidization. If it does, those funds for the purpose of cross-subsidization can be extracted not only from AT&T but also all the other long-haul carriers simply by building a subsidy of such amount as was thought appropriate into the exchange access tariffs.

Senator SPECTER. Professor Baxter, anything may happen to the local rates, but at least the consumers know what the rates are now. Where you have this very sharp change in structure of AT&T and you have the local companies operating on their own and you have the possibility—in fact the projection by a great many experts—that the rates may well double, are not the odds a lot better in favor of the consumers if things stay as they are now that there will not be such drastic changes in rates?

Mr. BAXTER. No, I do not think they are. I think the projections of which you speak for the most part were made in the present structural context. Local rates are expected to go up under the present structural context.

Senator SPECTER. Not as much as doubling, are they?

Mr. BAXTER. Yes.

Senator SPECTER. Your expectation would be that telephone rates would double if settlement is not approved?

Mr. BAXTER. No; I did not say that. I said I have seen a number of people who regard themselves as experts and some who are regarded as experts by others project that local telephone rates will double. Those were projections made before anybody heard of this decree.

I do not know whether they are correct. I expect they will go up at least to the extent of inflation. If we continue to have 9 percent inflation, as, roughly speaking, we did during the past year, then everything will double during the next 7 years and the real cost of everything will remain the same.

Senator SPECTER. The projections as to the doubling of rates are really not on an inflation figure over a protracted period of some 7 years. The estimates of the doubling of rates are those occasioned by the divestiture in these settlement provisions.

Mr. BAXTER. To the extent they are based on divestiture or this settlement they are simply totally without foundation of any kind.

Senator SPECTER. As a matter of your own personal judgment, would you think it appropriate that the local PUC's should seek to use the variety of mechanisms that you have described to maintain the local telephone rates at about their current level plus inflation?

Mr. BAXTER. I do not have a view on that. That is primarily a matter of local regulatory policy, not a matter of antitrust policy, although I must say that my own personal view is that we would be better off if all goods and services in the economy were priced at prices that correspond with their costs.

I am not particularly sympathetic toward imposing a hidden excise tax on long distance telephone calls in order to subsidize local phone calls or the converse. Nevertheless, that is a matter of local regulatory policy. If a local public utility commission wishes to do that, we have created a mechanism through which they may do it in the decree.

Senator SPECTER. If your philosophy then is carried out and local telephone rates are based on their cost, there will be an enormous increase, will there not, considering the facts of subsidies about which you have already testified extensively today?

Mr. BAXTER. I do not know because I do not know how great the present subsidies are. I doubt frankly that anyone has a very clear picture of how big the present subsidies are.

As I indicated, there is one visible piece of the subsidy that occurs through the separations and settlement process which involves primarily a cost allocation with respect to nontraffic sensitive plant at the BOC level. There are also, however, the license contract fees which flow in the opposite direction, conceivably a premium of the sort that is built into the price of Western Electric equipment, which will disappear. Exactly how those things will net

out in the rearrangement I do not know. I do not think anyone else knows precisely.

I do know that if local rates go up, it will be because the local public utility commissions did not take advantage of the exchange access tariff to the extent they might have to keep them down further. In my view that would not make it an inappropriate thing to do.

Senator SPECTER. Professor Baxter, if you say you do not know even with approximations what the present subsidies are, is that not a major problem or perhaps more specifically a major failure in this kind of settlement proposal? What the court is going to do under the charge of the Tunney Act and what the Congress and the Senate should be doing here is to make an evaluation as to what the public impact is going to be.

The first question is going to be what will happen to the local telephone rates. In order to answer that question, we really have to know what subsidies there are at the present time in addition to the mechanisms which may be available for maintaining those subsidies for the future.

When you say you do not know what the subsidies are even in approximation, is that not really a major failure? Do you not have to know that before you can go forward with this kind of an enormous settlement proposal?

Mr. BAXTER. I do not think anyone knows with any precision. I can make guesses. I think there is a very substantial offset that is flowing back to the AT&T company through the license contract fees and prices of Western equipment which substantially reduce the number that is usually kicked around as coming out of the settlement process, but the accounting that is involved in ascertaining an answer to that question with any precision is so judgmental and so subjective that I do not think anyone can suppose he really has a confident answer to those questions with any precision.

What I do know is there is a mechanism within the control of the regulatory agencies which will permit them to achieve any relationship they wish to achieve between the relative cost of local service and the relative cost of long distance service.

Senator SPECTER. Mr. Baxter, when you talk about the subsidies in terms of precision, I can understand that. However, I would think that you ought to know and the Senate ought to know some approximation. That is a question which I for one will be asking the AT&T officials today. It may be that the information as to subsidies is better requested from them.

However, I would make the same request of you in terms of supplying supplemental factual information for the committee. I ask that of you based on my thought that it is something you ought to know yourself in terms of fashioning this settlement, because when you talk about what the local PUC's may be willing to do by way of subsidies, I think very relevant what the amounts of those subsidies are.

If they are relatively modest, I can see the PUC's saying,"We will extract something by way of the yellow pages or the access tariff from long distance to local service." But if they are gigantic, then I can see the PUC, in a free enterprise setting which the de-

regulation bill endorses and which this settlement really carries forward, saying, "No, the new mode is let the consumer beware."

I think the amount of the subsidies would be very important in reaching a judgment on the quality of this kind of a settlement.

Mr. BAXTER. The amount of the subsidy, whatever that amount is, is presently being extracted from the long distance service through this cost allocation process that I have described. It follows necessarily that it cannot be too big to be extracted from the long distance service through exchange access tariffs so that nothing need change in that respect.

Senator SPECTER. Professor Baxter, a question was asked about Southern New England Telephone Company and Cincinnati Bell. Since 1956, the decree bars AT&T from buying such telephone companies. The new decree abandons that restriction. Is there anything legally or technically which would bar AT&T now from acquiring those two telephone companies?

Mr. BAXTER. I do not think there is anything. I must confess that that is not a question that has occurred to me before. I would want to sit down and read the proposed modification with that very question in mind. My offhand reaction is that, no, there is nothing that would keep AT&T from doing that.

I would be very surprised if they found that an attractive course at this point in time. Indeed, I am not sure I would find it very troublesome if they had such a small foothold in telephone service as that would represent. However, I must say I am not absolutely confident of the answer to your question either.

Senator SPECTER. Professor Baxter, it might be of surprise to you, but it would be of even greater surprise to the users of those two companies if they suddenly found AT&T owning their companies in the face of this divestiture which is supposed to leave AT&T out of operating companies.

Our review shows that there is nothing to stop AT&T from buying those two big companies. I would ask you if it would not be consistent with the approach you have had to divest the 22 local operating companies to make sure that AT&T does not have the power to buy them now and to do what it could not do under the 1956 decree because this changes the 1956 decree.

Mr. BAXTER. I understand the point. As I say, I would be amazed if that were a course of action that appealed to AT&T. I am sure their representatives would be able to give you much better answers than I in that respect.

Senator SPECTER. Would you not think it preferable to have the settlement arrangement preclude that possibility?

Mr. BAXTER. There are a wide variety of unwelcome events that I suppose might have been written into the settlement proposal. In the interests of keeping it short and as understandable as possible, my inclination was to preclude only those events which I thought at least moderately likely. I think that one most unlikely.

Senator SPECTER. However, you did not preclude events you did not think of.

Mr. BAXTER. No.

Senator SPECTER. That was one of them.

Mr. BAXTER. No. We discussed that problem.

Senator SPECTER. You discussed those two telephone companies?

Mr. BAXTER. Yes.

Senator SPECTER. I thought I understood you to say you had not considered whether they could buy those companies under the settlement decree.

Mr. BAXTER. I did not consider whether they could buy up the remaining interests in those two companies under the decree, but the status of those companies was discussed.

Senator SPECTER. Let me conclude this line by simply requesting you to consider further with AT&T at least on my thought that it would be in the public interest if the possibility were eliminated that AT&T could acquire those two companies.

Professor Baxter, with respect to the thrust of a letter which you sent to David Stockman on May 27, 1981, concerning the prospective testimony of Secretary of Commerce Baldrige, you made a point at the start of this very complex and comprehensive letter that there ought to be a separation of AT&T's participation in regulated and unregulated markets.

Since you project that it may be as long as 7 years before long distance lines may be unregulated, would it not be preferable, so long as the long distance lines are in the regulated category, to sever those as well from AT&T as you have severed the other regulated aspects of AT&T's business?

Mr. BAXTER. I do not think so. As I have already indicated, one must make a distinction between three different concepts. An activity can be regulated even though it is not a natural monopoly. A company can have a very large market share without having a significant degree of market power.

I think the Long Lines Division has and will continue to have a large market share. It is, and for some period of time will continue to be, regulated. However, it is not a natural monopoly. It has no statutory entry barriers. I think its potential for cross-subsidization is quite limited and will become even more limited rather quickly with the passage of time.

Therefore, I do not see the retention by AT&T of the Long Lines Division as representing the kind of problem that was represented by their affiliation with the basic operating companies.

Senator SPECTER. Do you think it has any potentiality at all for cross-subsidization?

Mr. BAXTER. I think it has modest potentiality in the immediate future. However, I think there are other things to be taken into account, too. I think the essentiality of the affiliation between Western Electric and the Long Lines Division and the Bell Laboratories in the perception of the Department of Defense as a military defense and emergency preparedness need is quite important in that context.

Senator SPECTER. On that subject, were the top officials at the Department of Defense consulted with respect to this settlement arrangement?

Mr. BAXTER. Certainly, they saw the arrangement before it was announced.

Senator SPECTER. Did you consult with them personally?

Mr. BAXTER. I did not personally.

Senator SPECTER. Who handled that aspect of the matter if you know?

Mr. BAXTER. Officials from AT&T.

Senator SPECTER. On that subject, I note that Judge Greene, in his order of January 21, has required that within 15 days the defendant shall file with the court a description of all contacts between AT&T and anybody in the Government, except for the limited contacts between counsel of record and officials of the Justice Department.

Do you know of any contacts which were made by AT&T with anybody in the Government relating to the settlement of this case?

Mr. BAXTER. The only contacts of which I am aware were contacts which I requested be made with the Defense Department and with the White House after the decree had been worked out in substance so that they would be informed and so they could express any residual concerns they might have about defense and emergency preparedness needs that we had not taken care of, notwithstanding that we made an effort to take care of all such needs.

Senator SPECTER. Professor Baxter, why did you leave that to AT&T officials instead of having you consult with those officials, who are really much more in the category of your client as attorney for the Government?

Mr. BAXTER. The only answer I can give you now is that things were getting quite pressed then. I was just about to go out of the city for a period of days. We decided to handle it that way.

Senator SPECTER. I must confess I do not understand that. Are you saying you did not have time or did not have somebody to whom you could delegate the function of talking to other Government officials so that you left it up to the opposing party in the case?

Mr. BAXTER. Yes.

Senator SPECTER. Why?

Mr. BAXTER. Without slowing the process down it would not have been possible for me to go do that. We were working on a very compressed schedule. I was out of the city. We had the long weekend. Then it carried into the week of January 8. I was in Salt Lake City where I had promised to give a speech a long time before. It would have slowed the process down.

Senator SPECTER. Is it not true that the settlement was pretty well worked out by December 31 on the date when you issued the press release?

Mr. BAXTER. No. There was a lot to be done from that point on.

Senator SPECTER. At what point did you have a settlement which was sufficiently definite so that the occasion would have been ripe to take it up with members of the administration, Defense Department or otherwise?

Mr. BAXTER. It is difficult for me to be sure without a calendar in front of me, but I think probably it was Monday. That must have been January 4 or 5.

Senator SPECTER. January 4, Monday, or Tuesday, January 5?

Mr. BAXTER. Yes.

Senator SPECTER. What was it specifically about your schedule that precluded your taking it up with members of the administration?

Mr. BAXTER. I was already on the west coast at that time. I had an obligation to attend some seminars in Salt Lake on the night of the 6th and the day of the 7th.

Senator SPECTER. Was not the issue of communicating to other officials in the Government a much more important matter than any of those items?

Mr. BAXTER. It certainly was. I could have canceled them. I also saw no reason why those contacts could not as well be made by AT&T officials.

Senator SPECTER. Mr. Baxter, when you talk about those contacts and say you saw no reason why they could not as well be made by AT&T officials, do you not consider it highly unusual for a lawyer to have the other side communicate the terms of a settlement to people who are essentially his clients on a very important litigation matter?

Mr. BAXTER. It is unusual to be sure. The terms were all written down. I had no doubt that they would be accurately conveyed. The AT&T people had well-established relationships with the Department of Defense, which was one of their stops. I just saw no particular reason not to handle it that way, unusual though it is to be sure.

Senator SPECTER. Professor Baxter, just as you have never seen a litigation matter where a litigator thought he was going to lose, have you ever seen a litigation matter where the lawyer sent his opponents to talk to his client about a settlement?

Mr. BAXTER. I have only recently seen this one. I do not believe I have seen any other one.

Senator SPECTER. I have seen a lot of litigation matters and have been involved in a lot of them. I have never seen one where the lawyer sent the other side to talk to his client. I find it very unusual, really highly unusual.

Did you not have other staff members? You had other people who worked with you. The press carries accounts of two other lawyers who worked with you on the drafting of the stipulation. Were not either of those men available to confer with your clients?

Mr. BAXTER. Yes, they would have been available. They were here in the city working on aspects of this case, but I did not ask them to go.

Senator SPECTER. Why not?

Mr. BAXTER. Because it seemed to me that the AT&T officials could do that job fully well. There were a large number of things to be done. That was an important one. I expected that they would be fully capable of taking care of that problem.

Senator SPECTER. Do you not have more confidence in your own assistants on a matter of dealing with the case than you do with an opponent?

Mr. BAXTER. Yes. However, I had sufficient confidence in the AT&T officials that they would do this particular job.

Senator SPECTER. Mr. Baxter, what would the consequence have been had these so far unidentified Government officials disagreed with the settlement?

Mr. BAXTER. The people at the Defense Department?

Senator SPECTER. I do not know. That is one level of people. Who were they?

Mr. BAXTER. Although you really should ask the people with the firsthand knowledge——

Senator SPECTER. I will do that.

Mr. BAXTER. I believe they contacted the Secretary of Defense and counsel for the President in the White House.

Senator SPECTER. Who made those contacts on behalf of AT&T? Did either Mr. Tanenbaum or Mr. Trienens? They are our witnesses this afternoon.

Mr. BAXTER. I believe the chairman, Mr. Brown, was along. I do not know whether either Mr. Trienens or Mr. Tanenbaum accompanied him, but, as you say, they are here and will be able to answer that.

Senator SPECTER. At any rate, they talked to Secretary of Defense Weinberger as you understand it?

Mr. BAXTER. As I understand it, Mr. Brown talked to the Secretary of Defense.

Senator SPECTER. Any others at the Department of Defense to your knowledge?

Mr. BAXTER. I do not know.

Senator SPECTER. Who else in the administration, if anyone, to your knowledge?

Mr. BAXTER. The counsel to the President, to my knowledge.

Senator SPECTER. Mr. Fielding?

Mr. BAXTER. Fred Fielding.

Senator SPECTER. To your knowledge that is all?

Mr. BAXTER. To my knowledge.

Senator SPECTER. What would the consequence have been had any of those individuals, that is Mr. Fielding or those at the Department of Defense, objected to the proposed settlement?

Mr. BAXTER. I would have felt obliged to delay any announcement, to take into account the grounds of their objection, and to see if the decree could have been adjusted to take care of it.

Senator SPECTER. This brings up the question that you and I have discussed at some length in the past with respect to the statute which precludes anyone except the Department of Justice from settling litigation. The specific provision I refer to is the one in 28 U.S.C. 516 which provides: "Except as otherwise authorized by law"—there is no other relevant provision here—"the conduct of litigation in which the United States or an agency or officer thereof is a party or is interested and securing evidence therefor is reserved to officers of the Department of Justice under the direction of the Attorney General."

In light of that statutory provision, Professor Baxter, what do you think the appropriate role would be for Mr. Fielding or Mr. Weinberger, if any?

Mr. BAXTER. I believe that as to the question of liability, the prosecution of the case, and with respect to liability, they had no appropriate role. However, with respect to the relief sought in the case, since the defendant in the case is to a very major extent the communications network of the United States, the White House, as advised by the Department of Defense, is entitled to have a general telecommunications policy consistent with its defense and emergency preparedness objectives and it was entirely appropriate for them to caution me, as they did on several occasions, that in any attempt

to settle this litigation or, indeed, in seeking relief should it go all the way through the court system, I should have very much in mind the possible impacts on national defense and emergency preparedness.

I attempted to do that. I had many discussions with the Department of Defense over the months as to what those concerns were. In working out the decree, I tried to be sure that we had a decree that took care of those concerns. As a last check, I asked if the AT&T officials would be sure that the Secretary of Defense and also the White House got a look at it before we made any announcement to see that it did meet those concerns. They agreed to do that and we went forward that way.

Senator SPECTER. Professor Baxter, in light of not only the importance of this settlement but in light of the statutory provision which I just read, did the thought not cross your mind that this would be a uniquely important matter on which for you personally or one of your top assistants to confer with those high-ranking Government officials to see if they agreed with this settlement?

Mr. BAXTER. I conferred afterwards on my way back from Salt Lake on the afternoon or evening of January 8. I conferred with counsel to the President to make sure that the contacts that I had contemplated would be made had in fact been made and that there was agreement that the proposed modification we had drafted did in fact meet those defense and emergency preparedness needs.

Senator SPECTER. Did you confirm that with Secretary Weinberger, as well?

Mr. BAXTER. No. I confirmed that with Mr. Fielding.

Senator SPECTER. That was on the 8th after the settlement had already been publicly disclosed and the court proceedings occurred?

Mr. BAXTER. No.

Senator SPECTER. Earlier in the day than that had happened? The 8th was the day when the proceedings occurred.

Mr. BAXTER. Was the 8th a Friday?

Senator SPECTER. Yes.

Mr. BAXTER. Then it was the night of the 7th on my way back to Washington before there had been any announcement.

Senator SPECTER. You say you had the press of these other commitments, the seminars and obligations in the western part of the country, but what was the emergency or necessity for such haste to get this matter concluded by the 8th when the case had been pending since 1974?

Mr. BAXTER. There was no great emergency. Trial had been in recess. We were going back into a trial period. It was very expensive. Once we began negotiating in this vein and once it became apparent that we probably could work out something, our effort was to see if we could not get something worked out so it would not be necessary to resume the trial phase of the case.

Senator SPECTER. Therefore, it really would not have made a great deal of difference in your judgment if it had taken a few extra days?

Mr. BAXTER. It would not have been monumental in its importance, no.

Senator SPECTER. Did not the lack of any emergency situation bear on your decision to let the AT&T officials talk the case over with your clients?

Mr. BAXTER. No; I really did not regard that as so extraordinary a step as you obviously do regard it.

Senator SPECTER. Was there any effort to get this case settled on the 8th in advance of the matter being called to Judge Greene's attention? Perhaps a preliminary question would be better: When was Judge Greene scheduled to return?

Mr. BAXTER. As I recall, trial was scheduled to resume Tuesday the 12th. If it was to be settled before trial resumed, it pretty much had to be settled on Friday. I had to fly to London on Monday and was in Europe for all of that week. That would have carried us clear through the first week of trial before I would have been able to return from that trip.

Senator SPECTER. Then you are saying that the events of the 8th were in no way tied to Judge Greene's unavailability on that day?

Mr. BAXTER. No.

Senator SPECTER. Was he in fact unavailable on the 8th?

Mr. BAXTER. I have no idea.

Senator SPECTER. Was there any effort made to communicate to Judge Greene the substance of the settlement of the case over which he was presiding before it was announced on Friday, January 8?

Mr. BAXTER. As opposed to filing it in the clerk's office, I do not know. Early on the morning of the 8th lawyers went to the Third Circuit to dismiss the appeal from Judge Biunno's interpretive order in the 1956 case. Lawyers went to Newark, N.J. to file the modification in New Jersey and to move to transfer the New Jersey proceeding down to Washington. Lawyers went to the Federal District Court in Washington to dismiss the 1974 case.

Senator SPECTER. All the lawyers were busy? No one could go see Judge Greene?

Mr. BAXTER. When the matter was brought to the personal attention of Judge Greene, which I am sure it must have been on the 8th, I do not know. I do not know that exact time.

Senator SPECTER. The procedural status of the case is an unusual one in that the documents were presented to Judge Biunno on the 8th. Judge Biunno held a hearing on the 11th for which there is a transcript. On the 11th itself Judge Biunno enters a very extended opinion which makes it apparent that Judge Biunno could not have prepared his opinion subsequent to the hearing. It has all the earmarks of very substantial preparation.

Then Judge Greene entered an order on the 21st vacating Judge Biunno's order. The matter is replete with the complex legal questions whether the Tunney Act applies to the modification of the 1956 decree, whether the Tunney Act is required in order to dismiss the case before Judge Greene, and the statements by the Department of Justice and AT&T officials that every expectation was present to have the Tunney Act applied notwithstanding the provisions of the law.

Was there any effort made in all of these proceedings to try to have the die cast before the case came before Judge Greene?

Mr. BAXTER. I am not sure I know what you mean by the die cast.

Senator SPECTER. The matter dismissed by Judge Biunno before the matter came before Judge Greene.

Mr. BAXTER. No.

Senator SPECTER. You had in this case a settlement proposal under rule 41 where the representation is made that court approval is not necessary.

Mr. BAXTER. Court approval is not necessary under a rule 41 dismissal. Is that what you are saying?

Senator SPECTER. No; that is not what I am saying at all. That was the effort which was made, to have a dismissal filed under rule 41 without court approval.

Mr. BAXTER. It was filed under rule 41.

Senator SPECTER. No, it was not filed; it was lodged. Judge Greene refused to accept it as filed.

Mr. BAXTER. Yes; I understand.

Senator SPECTER. That made quite a difference.

Mr. BAXTER. In my view it makes no difference.

Senator SPECTER. When you say you understand, Professor Baxter, I understand what you are saying. It is a reply. However, the procedural snarl is really very substantial. You think it makes no difference if the dismissal is lodged as opposed to filed.

Mr. BAXTER. That is correct.

Senator SPECTER. You disagree with Judge Greene.

Mr. BAXTER. In that very limited respect.

Senator SPECTER. Were you surprised, or what was your reaction when you noted that Judge Greene vacated the order of Judge Biunno?

Mr. BAXTER. I was not surprised. I was pleased. We had urged him to do that. We did not want Judge Biunno to enter his order up in New Jersey. We were surprised when he undertook to do that. We had hoped to have the case transferred down here with the modification merely proposed. Judge Biunno surprised us by entering an order approving it.

That also had the consequence of setting the clock running on the 6-month provision and the 18-month provision when we were still contemplating substantial hearings in Washington so that other parties would have an opportunity to make their views known. When we succeeded in getting the case transferred down here, we suggested and welcomed the vacation of the order entering the proposed modification and starting the clock running.

Senator SPECTER. You say, suggested to Judge Greene that Judge Biunno's order be vacated?

Mr. BAXTER. Yes.

Senator SPECTER. Where did that occur? It did not occur in the proceedings of January 12 before Judge Greene.

Mr. BAXTER. I cannot tell you the exact answer to that, Senator. I mean, I do not go over to the courtroom myself for many of these things. I asked my attorneys to suggest to Judge Greene that we would welcome a vacation of that order. Then there was a vacation of that order. It is even conceivable that Judge Greene went right ahead in doing it and we never had the opportunity to make the suggestion I had instructed be made.

Senator SPECTER. You say it would be conceivable?

Mr. BAXTER. It is conceivable. However, I had assumed that we had, in fact, made our suggestion and then the vacation order had come. Certainly, I gave the instructions that it was to be suggested.

Senator SPECTER. Based on the tenor of Judge Greene's comments at the January 12 hearing, it would not be surprising to me that Judge Greene would have vacated Judge Biunno's order without an application.

I would be interested to know, Professor Baxter, if any formal motion was filed or if any formal request was made. I have never seen one. I am not sure we have all the legal papers, although we have made an effort to collect them.

Mr. BAXTER. I will check on that. I think perhaps it was simply an informal suggestion to the judge.

Senator SPECTER. Professor Baxter, with respect to the current provision of rule 41, do you think it desirable that a case like the AT&T case should be dismissible without a legal requirement of submission to the Tunney Act?

Mr. BAXTER. I missed one word in that question.

Senator SPECTER. I would be glad to repeat it.

My question is: Do you think it is desirable that rule 41 authorize a dismissal of this AT&T case on the stipulation of counsel without a binding requirement of submission to the requirements of the Tunney Act?

Mr. BAXTER. The word desirable is what I missed.

That is a very complex question. I think it is desirable that there be a rule 41 that reads the way rule 41 reads and the parties be able to dismiss a case by stipulation without the concurrence of the judge.

I think it would be a mistake to read the Tunney Act to apply to stipulated dismissals of antitrust cases in any general sense, or, indeed, to modifications because so many of them will be trivial and will not warrant Tunney Act type procedures.

On the other hand, in a case of the magnitude of AT&T, it would seem to me troublesome and would justify the procedures contemplated by the Tunney Act to bring that act to bear, but I do not think the act applies to dismissals or to modification. I think it applies to what it says it applies to, to consent decrees.

In this case, since in substance we were doing very much the same thing and are going to have a proposed modification in front of Judge Greene, the issue really was not raised for us. We said it does not apply, but we are going to get this modification filed up in New Jersey, then transfer it down here, and there will be a case back in front of Judge Greene before he even expresses surprise with the rule 41 motion. We will follow the substance of the Tunney Act procedures with no problem. That is exactly what we have done.

Senator SPECTER. Professor Baxter, the language of rule 41 says that the Tunney Act applies to any proposal for a consent judgment. Do you know of decided cases which say that the language I just read does not apply to a stipulation of dismissal entered into between counsel?

Mr. BAXTER. I do not believe there is any case authority on that proposition.

Senator SPECTER. Should it be possible to circumvent the provisions of the Tunney Act which require a hearing in the public interest by simply denominating a document as a stipulation of dismissal between counsel which would have all of the same purposes of a consent decree but would simply change that kind of language?

Mr. BAXTER. I would not think it would have all the same purposes of a consent decree. A consent decree usually imposes some sort of injunctive or structural remedies on a defendant. It attempts to change the industry in some respect. Rights of third parties are likely to be affected in some way.

A dismissal is simply a dismissal. It does not change the industry. It simply says we are going to stop litigating and the industry will go on as before.

Senator SPECTER. In this case, the dismissal was really premised on these structural changes. You were able to avoid the consequence of the Tunney proceeding before Judge Greene by carrying it out before Judge Biunno.

Mr. BAXTER. We had never contemplated carrying it out before Judge Biunno. We contemplated filing it up there and then filing a joint transfer motion, which is also not within the discretion of the judge.

Senator SPECTER. However, no such motion was filed.

Mr. BAXTER. Yes, it was, Senator.

Senator SPECTER. I stand corrected.

Mr. BAXTER. We filed a joint motion to transfer the case simultaneously with filing the modification in New Jersey. To our surprise, amazement, shock, and horror, Judge Biunno entered the proposed modification and delayed the transfer.

Senator SPECTER. Risking asking for speculation of the mind of another but realizing you were a litigant in that court for some time, why do you think he did it?

Mr. BAXTER. I have no explanation for that.

Our purpose was simply to get the whole matter before Judge Greene in this form. We did not do it in order to avoid the Tunney Act. We had no purpose to avoid the Tunney Act. We were going to follow the substance of the Tunney Act, but we had to get the two cases together in some one place in order to have a sensible consolidation and windup. Judge Greene was obviously the right place. Then the question arose as to how do you get them both together before Judge Greene. This seemed to us the right way to do it.

Senator SPECTER. Why did you not simply file the settlement agreement before Judge Greene and ask for a consent decree there?

Mr. BAXTER. Because then we would have had an independent proceeding still trailing up in New Jersey.

Senator SPECTER. Then you could have asked for a tranfer at that time.

Mr. BAXTER. We could have, but we would have had to go through very much the same thing. We would have had to go to the third circuit and dismiss the appeal from the interpretative order and get the case transferred down from New Jersey. They were closely analagous alternative procedures.

Senator SPECTER. Professor Baxter, on page 6 of your written testimony today you say that the reorganization achieved by the modification of the 1956 decree is nearly identical to the relief that had been sought by the Department of Justice. In what respect was it not identical?

Mr. BAXTER. I have not looked back over the prayer for relief in the last few weeks. There are several references in there to possible divestitures of Western Electric and other possible forms of structural relief than the one which was our primary prayer for relief and the one we got.

Senator SPECTER. Is that the same reasoning which was behind the language in the other part of the sentence on page 6 that, together with the injunctive provisions, the modification substantially achieves the purpose of the 1974 case?

Mr. BAXTER. Yes.

Senator SPECTER. Nothing more was intended by the use of the language "nearly" or "substantially" than what you have just recited?

Mr. BAXTER. Right. It is not precisely what we asked for in the relief contentions in the case, but the differences are not significant.

Senator SPECTER. Professor Baxter, how is Judge Greene to rule within 60 days on the proposed settlement when AT&T will not have submitted its proposals to the Department of Justice until after that date?

Mr. BAXTER. It is not entirely clear to me when AT&T will have its proposed reorganization available.

Senator SPECTER. What is its obligation?

Mr. BAXTER. Its obligation is to have it within 6 months.

Senator SPECTER. It is entirely likely that he will not have it then within 60 days.

Mr. BAXTER. It is entirely possible.

Senator SPECTER. If that sequence follows, how can Judge Greene make a determination of public interest in the proceedings in his court if he does not have the AT&T proposals before him?

Mr. BAXTER. I do not know. He may find that difficult. I would have thought that the decree, although it is quite general in many respects, blocks out the central themes of reorganization. I would myself think that more emphasis than was appropriate was put on the reorganization proposal if he were to find that he really had to see the details of the reorganization proposal before he entered the approval, but he may come out in that place.

Senator SPECTER. Does he have the authority under the Tunney Act proceedings to delay his judgment beyond 60 days?

Mr. BAXTER. Certainly he has the authority not to approve the proposed modification.

Senator SPECTER. That puts you back to square one then, does it not?

Mr. BAXTER. There is no question that the judge can put us back to square one.

Senator SPECTER. My question turns on the timetable. You have the Tunney Act in 60 days. You have the submission by AT&T in 6 months. You have the provision that it is to be acceptable to the Department of Justice. Why to the Department of Justice and why

not to the court? Is that a function really which the Department of Justice ought to pass on without review by the court? Would it not be more appropriate in line with the theory of the Tunney Act to have it subject to a public interest determination by the court?

Mr. BAXTER. That is a perfectly arguable position. It seemed to us that the features of the reorganization were not likely to be terribly controversial. I understand that many people think it is much more critical than that.

In any event, we wrote it the way we wrote it and as of this time it calls for approval by the Department of Justice. I obviously contemplated that in making that approval we would seek advice from a variety of expert sources, but it still seemed an appropriate way to handle it.

Senator SPECTER. Is it your judgment that Judge Greene will have jurisdiction to defer a final adjudication on the settlement proposal until after 6 months may expire and AT&T makes a submission?

Mr. BAXTER. I have not researched that particular point, but I would be astounded if some procedural device that produced that result could not be found.

Senator SPECTER. On your contest of the requirement to submit to the Tunney Act for the modification of the decree, which I understand you are litigating in the ninth circuit, do you think a rule might be fashioned which would subject modification of a decree to the Tunney Act provisions which could separate out the lesser matters that would be burdensome from the major ones like the one at hand?

Mr. BAXTER. I think that would be difficult to do. My inability to think of any very satisfactory way one could articulate such a separation of proposed modifications into the trivial and the important has led me to take the position that the Tunney Act simply did not by its terms apply. However, wherever significant matters were involved, we would simply encourage the judge to hold hearings and follow its procedures in substance.

Senator SPECTER. Professor Baxter, that may be an adequate procedure so long as the antitrust division is in such fair and judicious hands, but the issue arises as to what the law requires. I for one would appreciate it if you would give consideration to some description which might separate out lesser modifications from major modifications. I think this case raises the issue very boldly.

As you note, this is one which really ought to have the protection of the Tunney Act. It ought not be left to the high integrity and high standards of the particular assistant attorney general in charge.

I would also ask you, if you would be willing to do so, to give consideration to the possibility of a workable modification to rule 41 which would require Tunney Act application where there is a stipulation of dismissal because, although there are some significant differences in terms of court enforcement of the dismissal and retention of jurisdiction, that certainly is an avenue where the parties can avoid the requirements of the Tunney Act if you read rule 41 as narrowly as you have suggested.

Mr. BAXTER. I have considerable sympathy with your first suggestion about modifications. I will try to give that more thought.

I really do not think I agree with you, Senator, on the rule 41 point. In the kinds of instances where you would invoke a rule 41 dismissal, you are not doing the kind of thing that the Tunney Act was intended to guard against in my view.

Senator SPECTER. I respectfully disagree with you about that. Maybe it would be an appropriate subject for consideration by the Senate. I can pursue that independently, but I would certainly welcome your thinking along that line.

Mr. BAXTER. Surely.

Senator SPECTER. Professor Baxter, the hour is late. It is not that my questioning has been more extended than others, but with my lofty seniority it comes at the very end.

I will condense the questioning I have on the IBM question essentially to one question. That will require a bit of a preface. I will try to get you out of here by 1:30 because I know it is very late.

In the light of your testimony and in light of the standard that a prosecuting attorney has not to be the judge in the case but to exercise discretion in bringing the case and perhaps in dismissing a case—although I think the standards are different—as I read through your testimony, at page 13 you say, "Thus it was far from clear that we would win this case," raising the implication that although far from clear that was a distinct possibility; and at page 14 you say, "Had there been substantial factual and legal merit in the case I would have ordered its continuation notwithstanding its expensive history," indicating that there was some suggestion of factual and legal merit, albeit not substantial as you saw it; and on page 11 where you refer to, "At least by today's legal standards the theoretical underpinnings of the *IBM* case were uncertain, indicating that although underpinnings uncertain there were at least some underpinnings; and later at page 11 you refer to the nexus being problematic, indicating some advantage that there was some nexus; and on page 12, when dealing with the interface issue, you said it arguably represents improvements in the designs of the system."

All through your testimony you very carefully leave a substantial range of likelihood, or at least possibility, that the case might have been won had it been pursued to a litigation conclusion.

I see you nodding in the affirmative. Do you think there was at least a possibility that the case might have been won by the Government?

Mr. BAXTER. I was nodding in the affirmative because I understand exactly what your question was, not because the answer in my view was yes.

Senator SPECTER. Fair enough.

Mr. BAXTER. That is a very difficult question to answer. How could I say there was not 1 chance in 10,000 that that particular judge on some particular day might not be persuaded?

However, I think that is sort of the right order of magnitude. On every one of these points there could be legitimate doubt raised. Yet almost all of those doubts had to be resolved serially in our favor in order to win the case.

Then when we get all through with another 1½ of the judge coming in with an opinion, 3 more years of hearings on relief, and then there was an appeal to the second circuit which had already

decided *Berkey* v. *Kodak*, which is substantially inconsistent with the theory underlying the *IBM* case, on my really bad nights I can imagine the *IBM* case being remanded for retrial in 1990 on the basis of a record that started in 1959.

Senator SPECTER. Do you expect to serve beyond President Reagan's second term?

Mr. BAXTER. I have great empathy with my successors.

Senator SPECTER. How about your predecessor like Sanford Litvack?

Mr. BAXTER. Sandy was in the course of reviewing this case. I do not purport to know what judgment he would have reached.

Senator SPECTER. Did you talk to him about it?

Mr. BAXTER. No.

Senator SPECTER. I note you refer to his handling of the matter in your statement. At page 9 you say that the second circuit suggested settlement would be in the best interests of all concerned, but the second circuit did not suggest dropping the case.

Mr. BAXTER. No, it did not.

Senator SPECTER. The case had passed the procedural step where a motion to dismiss was denied at the conclusion of the Government's case.

Mr. BAXTER. Yes, it had.

Senator SPECTER. Was that not a weighty factor to be considered by you that, essentially speaking, the trial judge had come to a different conclusion than you had, or do you think it would have been sufficient for his purposes for him to conclude there was 1 chance out of 10,000 that it might be won and so he let the case go on?

Mr. BAXTER. I think it was permitted to go on under a very loose standard.

Senator SPECTER. A very loose standard?

Mr. BAXTER. "Permissive standard" would perhaps be a better word.

Senator SPECTER. Professor Baxter, that is what gives me pause about the case. I do not know the details of the case, but here we have a matter which has been in litigation for 13 years. Here we have a new Attorney General in charge of the Justice Department and an Assistant Attorney General who has very forcefully said that he disagrees with what the antitrust law has been interpreted to be in the past. This is a matter of dialog between you and this committee and you and me over some protracted period of time.

You have disagreed with your predecessor. You have disagreed with the judge who overruled a motion to dismiss. Now you have decided unilaterally. With all due respect to the power you possess, notwithstanding all the limitations which you have in your testimony, why is this a desirable procedure—with the enormous sums of money already spent, with all of those who have disagreed with you, with your own concession that you have a different view of the antitrust laws—that this power should be in your hands to say this case does not go forward when it is so close to conclusion?

Mr. BAXTER. No, it is not close to a conclusion, Senator. We are at least 6 months away from submission to the judge. Let me say 4 months away from submission to the judge, a year and a half away at the earliest from decision by a judge, 5 years away from disposition of the relief phase, 6½ years away from an opinion by the

court of appeals. We are a long way away and there are enormous resource expenditures to be made between here and there.

Since I have been unable, and, indeed, no one has been able, to suggest any relief in the case that seems at all plausible or even remotely likely to improve the performance of the industry, since I think that there is little evidence that anyone could plausibly find that had a causal connection with the maintenance of IBM's monopoly position, I decided not to make those continuing resource expenditures.

All the things you say are quite true. A lot of people have disagreed. Elements of my trial staff disagreed, although other professionals at the Department who reviewed the case and were not so closely involved in its ligitation over the years agreed with me, but there was no question that there was disagreement about that.

Senator SPECTER. You have just recited a chronology of 6½ years on a case which is already 13 years in the making. You are two-thirds of the way home.

Mr. BAXTER. That is about right.

Senator SPECTER. You could expedite that 6½ years. It does not have to take 5 years to the remedy stage.

Mr. BAXTER. I did not allocate 5 years to the remedy stage.

Senator SPECTER. I thought you did.

Mr. BAXTER. To the end of the remedy stage?

Senator SPECTER. I thought you said it would take 6 more months to finish the trial, a year for judgment, and 6½ years then to the remedy stage.

Mr. BAXTER. I thought I said 5 years, giving it another 3½ years.

Senator SPECTER. You might expedite that, ask for an expedited hearing. If you can apply some of the speed that you have on this settlement decree and perhaps delegate some of the work to the opposing counsel, maybe you can expedite it.

Mr. BAXTER. It is at least a theoretical possibility.

Senator SPECTER. Did the court enter an order of approval reviewing your judgment to drop the case, or was that unnecessary here?

Mr. BAXTER. It was unnecessary. The judge so explained to the press that afternoon.

Senator SPECTER. He was unhappy about your failure to appear personally in that proceeding?

Mr. BAXTER. He was.

Senator SPECTER. What was the reason for that if you know?

Mr. BAXTER. I was down here in Washington. Both cases were to be dismissed that day. I had dispatched lawyers to Philadelphia, Newark, N.J., and New York. I simply felt that I had to be here in Washington to make the announcements and to talk to the various then far-flung members of my staff as they called back in to say they had just filed the papers in the third circuit, in Newark, and so on and so forth.

Senator SPECTER. Are the reports true as noted in the media that it was just coincidental that IBM and A.T. & T. were settled on the same day?

Mr. BAXTER. Yes, it is true.

Senator SPECTER. We can at least thank the media for accuracy on that one limited aspect?

Mr. BAXTER. They merely reported accurately what I said.

What really forced them together was the two events that I referred to before. There was a whole week in which I had to be in Europe and a preceding week during which I had at least made commitments to be on the west coast. If it was going to come down anywhere in that 2-week period, it sort of had to come down on the 1 day I was back in Washington.

Senator SPECTER. Professor Baxter, what was the urgency? A.T. & T. had only gone on for 7 years, but IBM had gone on for 13 years. Could it not have waited another 2 weeks?

Mr. BAXTER. Yes, of course it could have waited, but both parties were in the process of preparing proposed findings of fact to be submitted to the court. Enormous efforts were being mounted to get those done by the 1st of February. Resources were being expended on the case at a very, very high rate.

Once I made the decision to do this, which I did probably over the Christmas holidays when I went through the papers for the very last time and said: "All right, this is what I am going to do," then I wanted to do it as quickly as possible to halt the very substantial devotion of resources to the process of preparing proposed findings which were being undertaken by both sides.

Senator SPECTER. Professor Baxter, as a matter of public policy, do you think it is desirable to lodge in one person, yourself, the authority to have a case dismissed without court approval where predecessor attorneys general in large numbers and Assistant Attorneys General of the Antitrust Division in large numbers and staff in large numbers all have reached a contrary conclusion?

Mr. BAXTER. I am not sure I really agree with all the recitals.

Senator SPECTER. Not all the whereas clauses?

Mr. BAXTER. Not all the whereas clauses. However, passing over the whereas clauses, I will say yes.

Senator SPECTER. It is desirable as a matter of public policy to lodge that much authority in one lawyer?

Mr. BAXTER. That authority of course is lodged in the Attorney General. It seems to me appropriately lodged with the Attorney General.

Senator SPECTER. Did Attorney General Smith review this matter with you?

Mr. BAXTER. No. He was recused. That of course is one of the oddities here, that both the Attorney General and the Deputy were recused. If you find it odd that that should be lodged with an Assistant Attorney General, I could agree completely.

Senator SPECTER. I do not find that odd. I do not make the distinction based upon the fact that you are an Assistant Attorney General as opposed to the Attorney General. My question really goes to the point of 13 years of litigation started by an Attorney General, reviewed by Assistant Attorneys General, reviewed by a judge a long way down the litigation path, staff which disagrees with your conclusions, and I am talking about an institutional matter and whether the Congress ought to allow this posture to remain, that one man in circumstances like these on a case of this importance can make a decision totally at variance with all the others in the chronology.

Mr. BAXTER. I really do not think there were that many considered decisions in the chronology, but that gets back to the whereas clauses.

Senator SPECTER. Even so, your answer is yes?

Mr. BAXTER. Even so, my answer is yes.

Senator SPECTER. The final question is: Given that as to IBM, do you think it desirable as a matter of public policy that the parties to litigation ought to be able to have a modification of a decree like the 1956 consent decree in the AT&T litigation without court approval, ought to have a dismissal of the AT&T suit pending since 1974 without court approval, and have the provisions of the Tunney Act to make an inquiry as to public interest only as a matter of the largesse of the Assistant Attorney General?

Mr. BAXTER. Again, I am not sure I caught all that.

Senator SPECTER. Let me break it up. You say you do not need court approval on a modification of a decree like the 1956 decree.

Mr. BAXTER. No; not at all.

Senator SPECTER. You say the Tunney Act provisions are not required on a modification of the 1956 decree.

Mr. BAXTER. That is correct.

Senator SPECTER. Except you agreed to it as a matter of your own largesse, as a matter of your own personal judgment.

Mr. BAXTER. As a matter of my judgment that it was an important matter and the kind of thing that Congress obviously intended to be treated as in the Tunney Act.

Senator SPECTER. However, if you had not decided that, the law did not require that the modification of the 1956 decree have the protective provisions of the Tunney Act?

Mr. BAXTER. I would have regarded that as an abuse of my discretion. Discretion is abuseable as well as properly exercised.

Senator SPECTER. Then the same thing follows that you could dismiss the AT&T suit pending since 1974 under rule 41 because of its technical provisions, as you have testified, without court approval?

Mr. BAXTER. Yes.

Senator SPECTER. My question to you is: Is that not too much power to vest in one man be he the Assistant Attorney General or the Attorney General, to have the authority to dismiss cases with the tremendous overriding importance of this litigation on his own say-so alone?

Mr. BAXTER. I do not think the power to dismiss a case is any more awesome than the power to commence a 13-year litigation. I cannot think why they should not be lodged in the same place.

Senator SPECTER. Why have the Tunney Act apply to any matter if you can say that if a case is begun by the Attorney General, by the logic you have just articulated, it ought to be dismissible by the Attorney General? The Tunney Act has no value at all by your rationale.

Mr. BAXTER. I think it is dismissible by the Attorney General. What cannot be done is to enter a consent decree because a consent decree is a very different animal and one far more likely to affect the rights of third parties than a dismissal. It does not seem at all surprising to me that Congress, when it passed the Tunney Act, made it applicable to consent decrees and not dismissals.

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Senator SPECTER. Final question: Do you think that all of these powers were properly useable by one man in two such big cases on the same day?

Mr. BAXTER. If they were properly done on different days, they were properly done on the same day.

Senator SPECTER. Thank you very much, Professor Baxter.

The hearing is now recessed until 2:30 when we shall take up the next two witnesses.

[Whereupon, at 1:40 p.m., the committee recessed, to reconvene at 2:30 p.m. the same day.]

[Prepared statement of William F. Baxter, plus answers to questions that were subsequently supplied for the record, follow:]

STATEMENT OF

WILLIAM F. BAXTER
ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

I am happy to be here today to discuss the recent actions of the Department of Justice regarding the AT&T and IBM cases. As you know, on January 8, 1982, the Department and AT&T filed an agreed-upon modification of the 1956 Consent Decree in United States v. Western Electric and AT&T, and stipulated to dismissal of the Government's monopolization case filed against AT&T in the District of Columbia in 1974. Also on that day, the Department stipulated to dismissal of the Government's monopolization case against IBM, a case that was filed in 1969, and that had been pending for some 13 years. The decisions to take these actions were clearly the most important that I have made as Assistant Attorney General. The dispositions of these cases are most significant. I appreciate fully the interest of the Committee in them.

The way in which we have moved to resolve our antitrust controversies with AT&T is one that I hope will be widely recognized as promoting competition in the dynamic telecommunications industry and as doing so in the most efficient way. While the modified Decree does not, and is not intended to, resolve all of the regulatory or legislative issues that may exist in telecommunications now or in the future, it does do what an antitrust decree should in these circumstances--eliminate the key structural barriers to the emergence of effective competition in the industry.

We had two litigation fronts open with AT&T, one involving a 25-year old decree that recently had been interpreted in a way that had substantial competitive ramifications, the other involving a monopolization case brought by the Government seven years ago, the trial of which was nearing completion. The restructuring of AT&T to which we have agreed, and the accompanying injunctions, resolve both of these controversies.

The 1956 Consent Decree was entered in settlement of an antitrust case filed in 1949 in New Jersey by the Department of Justice. That case charged AT&T with monopolizing the manufacture and distribution of telephone equipment in violation of the Sherman Act. Although the complaint in the 1949 case sought, among other things, the divestiture of Western Electric, the 1956 Decree did not require that divestiture. Instead, the 1956 Decree contained various restrictions on AT&T's activities, including limiting AT&T to providing "common carrier communications services," the rates for which are subject to governmental regulation. The premise underlying that restriction, I think, has been that absent such structural relief as would effectively eliminate AT&T's incentives and abilities to monopolize, confining AT&T to its traditional regulated common carrier communication businesses would ensure against AT&T subsidizing the provision of unregulated services and equipment with revenues derived from its regulated monopoly activities.

In September 1981, the U.S. District Court in New Jersey interpreted the 1956 Decree as permitting AT&T to offer certain equipment and services even though the rates for such equipment and services would not be subject to regulation. AT&T sought this interpretation after the FCC, in its 1980 Computer II decision, allowed AT&T to offer such equipment and services through fully separated subsidiaries. The Department appealed the district court's interpretation, but in conjunction with its agreement with AT&T on modification of the Decree moved to have the appeal dismissed.

Under the modified Decree, all of the provisions of the 1956 Decree would be eliminated and replaced by provisions requiring AT&T to undertake an 18-month reorganization, after which the Bell operating companies providing local exchange telephone services will be divested by AT&T into one or more companies. AT&T will continue to own a nationwide intercity network composed of its Long Lines Department and the intercity facilities of the Bell operating companies, and will retain ownership of Bell

Telephone Laboratories and Western Electric. AT&T will also provide customer premises equipment, including that now furnished by the local Bell companies. AT&T's plan for the required reorganization is to be submitted to the Department of Justice for approval within six months of the effective date of the modified Decree.

The modified Decree also requires the to-be-divested operating companies to provide, on a phased-in basis, exchange access to all intercity carriers equal to that provided to AT&T, and forbids the operating companies from discriminating against AT&T's competitors with respect to procurement, interconnection of equipment or services, the establishment and disclosure of technical specifications, and the planning of new facilities and services.

Let me explain the reasons for our seeking this modification. Any successful effort to establish a truly competitive telecommunications industry must prevent a dominant regulated carrier such as AT&T from frustrating the emergence of competition, particularly in telecommunications equipment, intercity services, and related information markets. AT&T's control of regulated local monopolies has enabled it to dominate intercity service and telecommunications equipment markets. Through its ownership of exchange monopolies serving 80 percent of the nation's telephones, AT&T has controlled facilities essential to any firm attempting to challenge Long Lines or Western Electric.

The most straightforward and effective way to eliminate AT&T's incentives and abilities to exclude competition from potentially competitive telecommunications markets is to require the divestiture of its regulated local exchange monopolies from those portions of AT&T that engage in competitive and potentially competitive activities. That is precisely what the reorganization required by the modification does. Divesting ownership of local exchange facilities from intercity facilities will eliminate the incentive and ability of a joint provider of local and intercity services to discriminate against other providers of intercity

services when such services must rely at some point upon the local distribution network. Similarly, the divested regulated operating companies would not have incentives to discriminate in favor of Western Electric and against other suppliers of telecommunications equipment. Because the divested operating companies may, for a period of time, retain some institutional loyalty and as a result of inertia continue to favor prior affiliates, the modified Decree establishes basic equal access and non-discrimination requirements to backstop the reorganization in promoting competition in intercity service and equipment markets.

The divestiture of AT&T's regulated local exchange monopolies that is accomplished by the modified Decree obviates the need for the restrictions that the 1956 Decree placed on AT&T. Without its base of regulated local exchange monopolies, there is no longer the same need to worry over the long run about cross-subsidized forays into unregulated markets and, therefore, no reason to restrain AT&T from entering such markets. To the contrary, enabling an enterprise with tremendous skills and resources to enter unregulated markets should increase competition and the pace of innovation in those markets.

We also believe that the modified Decree provides a framework for satisfaction of the concerns of the Department of Defense. Since early spring of last year when Secretary Weinberger, appearing before the Senate Armed Services Committee, indicated his concerns over the relief sought in the 1974 AT&T suit, we have had numerous meetings and discussions with DOD officials to discuss the specifics of our proposals and for us to learn their specific national security concerns. Under the modified Decree, national defense benefits from an integrated Long Lines, Western Electric, and Bell Labs will continue. In addition, the modification contains specific provisions to ensure continued centralized coordination among local Bell operating companies to meet national security and emergency preparedness needs.

Many have speculated that the restructuring required by the

modified Decree will necessarily lead to sharply higher rates for local telephone service as subsidies from long distance revenues are removed. In fact, the Decree itself will have no such effect. The current subsidy system would have been subject to some pressure from competition in long distance service in any event. Moreover, there is nothing in the modified Decree that would prevent federal or local authorities from generating a local service subsidy through local exchange access regulation. Indeed, the issue of whether to continue such subsidies is presently being reviewed by a joint federal-state board under the auspices of the FCC.

Agreement upon the modified Decree made it unnecessary to continue litigating the Government's 1974 monopolization case against AT&T. That case alleged that AT&T had monopolized certain telecommunications services and equipment markets. Trial began in early 1981 and was scheduled to resume on January 12 and be concluded in February. The reorganization achieved by the modification of the 1956 Decree is nearly identical to the relief that had been sought by the Department of Justice in the 1974 litigation, and, together with the injunctive provisions in the modification, substantially achieves the purpose of the 1974 case. Accordingly, the Government and AT&T stipulated to dismissal of the 1974 case without prejudice.

Concern has been expressed about the procedures to be followed in connection with the entry of the modified Decree. It is and always has been the intention of the Department, and AT&T, to follow the procedures of the Tunney Act in this matter, in order to allow opportunity for comment by others and a complete exposition of the modification's merits. The Decree will require a basic restructuring of the telecommunications industry, and thus necessarily affects vital public concerns. While we believe that the Tunney Act does not by its terms apply to modification of existing decrees, most of which involve minor adjustments of concern only to the immediate parties, the Act's procedures and standards can help facilitate thorough review of major decree modifications. Accordingly, we have followed comparable procedures

in connection with major decree modifications in the past.

It has also always been our intention to follow the Tunney Act procedures here in the District of Columbia. We believe that Judge Greene, who as a result of the trial of United States v. AT&T has substantial expertise in the telecommunications industry and the effects of restructuring, is uniquely qualified to make the determination that the modified Decree is consistent with the public interest. Therefore, upon filing the proposed modification in the U.S. District Court in New Jersey, the Government and AT&T moved to have jurisdiction over the 1956 Decree, and any proceedings relating to its modification, transferred to the District Court in Washington.

As the Committee knows, the District Court in New Jersey unexpectedly entered the modified Decree on January 11. While we appreciated that Court's view of the merits of the modification, we remained committed to thorough review in the District of Columbia using Tunney Act procedures. On January 14, 1982, Judge Biunno entered an order transferring the matter here. On January 21, 1982, Judge Greene, to whom the matter has been assigned, vacated the order entering the Decree and set out the procedures--identical to those of the Tunney Act--that he intends to follow. We intend promptly to take the steps required by Judge Greene's order. In short, we are following the Tunney Act path that we have intended to follow all along.

Finally, it is obvious that the changes in industry structure to be brought about by the Decree will have to be taken into account in assessing the need for and content of pending or future telecommunications regulation or legislation. Complex regulatory provisions designed to guard against anticompetitive cross-subsidization by AT&T are probably no longer necessary. There may be other issues not so directly related to competition that deserve regulatory or legislative attention--for example, the question of whether or how to subsidize local telephone service in a competitive environment--but I would defer comment on such matters at this time.

I would like to turn now to my decision to dismiss the Government's case against the International Business Machines Corporation. When I came to the Department in early 1981, I was only generally familiar with the case. I knew, however, of the public controversy as to its merits, and that it had consumed tremendous governmental, judicial, and private resources. I determined to make a decision about how to proceed with the case as soon as possible.

Some substantial efforts to review the case had been made not long before my arrival. In 1979, during the appeal of IBM's effort to remove the District Court judge from the case, the Second Circuit suggested that settlement would be in the best interest of all concerned. Not long thereafter, in November of 1979, the Antitrust Division assembled an internal task force of lawyers and economists to review the merits of the case with a view toward exploring different approaches to settlement. By the summer of 1980, this task force, aided by economic and technical consultants, completed its review of the merits of the case and various relief options. During the summer and fall of 1980, my predecessor, Sanford Litvack, met with the trial staff and with IBM counsel to discuss settlement possibilities. Nothing came of these discussions, however.

Upon my arrival in the spring of 1981, I reviewed the work that had been done on the case thus far. Between September and December of 1981, I held several meetings with the trial staff, alone and with counsel for IBM. I also reviewed materials submitted to me by the trial staff, the reports of the earlier task force, and met with senior Division attorneys and economists familiar with the case. I concluded that, in light of the state of the record and the state of the computer industry today, the case presented very substantial problems. There were problems with market definition, with evidence of bad conduct, and with relief.

In order to prove a violation of Section 2 of the Sherman Act, the Government has to define and prove the market that the

defendant is alleged to have monopolized. This task was made particularly difficult in the IBM case because the market continued to evolve as the case proceeded. The Government defined the market as that for large general purpose computer systems optimized for business use. This definition had become increasingly troublesome as computer systems became more powerful and were adapted to a greater variety of uses throughout the 1970s. The advent of distributed processing and the introduction of minicomputers with computing power comparable to that of the largest systems of earlier years created a definite litigation problem. The market we had defined had begun to seem either outdated or amorphous.

There were also theoretical and factual problems with our evidence of monopolizing conduct, or "bad acts." The theoretical problems of the case had been accentuated by recent judicial decisions that addressed the nature of the conduct that must be proved to establish monopolization. Briefly, the courts have shown a heightened awareness of the social benefits of aggressive competition, even by firms with large market shares, and an appropriate reluctance to equate such competition with the type of predatory practices condemned by Section 2. These courts, and I include the Second Circuit as evidenced by its decision in Berkey Photo */ in this category, rightly have begun to consider the consumer benefits of conduct that is alleged to have excluded competitors. At least by today's legal standards, the theoretical underpinnings of the IBM case were uncertain.

There were also factual problems with our evidence of bad acts. For example, perhaps the strongest evidence of predatory conduct concerned the prices IBM set for its System 360 Model 90 computer in 1964. Evidence introduced tended to support the conclusion that IBM set prices for this computer system at such a low level that the company did not realistically expect its

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*/ Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263 (2d Cir. 1979).

sales revenues to cover the costs of developing and manufacturing the machine. However, there were problems even with this episode. First, the 360/90 was not offered in the market we alleged to have been monopolized, that for general purpose computer systems optimized for business use. The 360/90 was a very powerful computer offered in the scientific market, a "number cruncher." Thus, the nexus between this pricing conduct and the maintenance of the monopoly we set out to prove is problematic. Also, there was relatively little evidence that IBM's pricing of the 360/90 was effective in maintaining monopoly power. It was offered in competition with Control Data Corporation's largest computer, the 6600; Control Data manufactured far more of these systems than did IBM.

By way of further example, there was also evidence that for competitive reasons IBM rushed to market its System 360 Model 67 computer system, its first model designed to offer time-sharing, and did so with an awareness that it might not be profitable. Here, however, the evidence of predatory intent was much more ambiguous than was the case for the Model 90. IBM believed it was very important to develop a time-sharing system, which was perceived as the wave of the future. Many of the problems IBM encountered with the Model 67 were unforeseen and were also experienced by its rivals. There was little evidence that IBM's conduct in this episode had the effect of maintaining its power in the market for general purpose computer systems.

Finally, there were allegations in the case that IBM changed the interfaces on its computer systems--the ways in which the various components in the systems were connected--in a manner intended to harm emerging competitors that offered peripheral computer devices designed to be used with IBM systems. The problems with this allegation arise from the difficulties in asserting that design changes in computer systems can amount to Section 2 violations when they at least arguably represent improvements in the design of the systems. The fact that four of the peripheral manufacturers themselves sued IBM on the basis of this evidence

and that IBM won all four suits certainly dampened whatever confidence the Division once had about prevailing on these episodes.

Thus, it was far from clear that we would win this case. Unfortunately, what relief we would seek if we were to win it was equally unclear. In a civil Section 2 case, there are two general types of relief that can be sought: injunctive and structural. Injunctive relief involves framing rules for the defendant to follow that are designed to prevent the illegal acts of the past and open the way to unfettered competition. The challenge in framing injunctions is to make them general enough to prevent easy evasion yet specific enough to amount to more than a simple restatement of the antitrust laws. Specific, detailed injunctions are particularly difficult to draw up in such an innovative and rapidly-changing field as computers. Such injunctions require continued monitoring and there is always a danger that regulatory-type injunctions may inject an artificial restraint that interferes with procompetitive responses to market forces. I do not believe that anyone ever proposed injunctions in IBM that would be both responsive to the evidence in the case and likely to improve performance in the industry.

The problems with possible structural relief in the IBM case were even more substantial. Structural relief involves realigning the structure of the defendant, most commonly, as in the AT&T modification, through the divestiture of assets. Structural relief in IBM likely would have involved splitting the firm up into two or more entities. The first problem with such an approach was that it seemed far out of proportion to any violation that we possibly could have shown. Also, in stark contrast with the AT&T situation, there was no obvious way to restructure the firm and thereby guarantee a procompetitive result. Splitting up an integrated firm of IBM's size, scope, and complexity would present mammoth practical problems. There is no assurance that a restructured IBM would perform more efficiently than it now does and there is a substantial possibility that it would perform consider-

ably worse. Structural relief in the IBM case seemed to me wholly inappropriate.

I thus was presented with a case that had dragged on for 13 years and was likely to continue for years more if the Government were to prevail, that was costing the Government millions of dollars, that was not proceeding in our favor, and that posed very substantial relief problems in any event. Had there been substantial factual and legal merit in the case, I would have ordered its continuation, notwithstanding its expensive history. While I believe that efforts to streamline such cases are important and should continue, I do not believe that the Government should shy away from meritorious cases because they may be complex, expensive, and time-consuming. I think the AT&T case shows that the Antitrust Division will continue to litigate aggressively when we are convinced of the merits of our cause, regardless of its complexity. In IBM, I was not so convinced.

It might have been possible in these circumstances to seek a cosmetic settlement with IBM, more as a face-saving gesture than anything else. However, I did not think that such a settlement would speak well for the integrity of the Department or serve the public interest. I therefore decided to dismiss the case. It was not an easy decision, but it was a decision on which I will stand.

Before closing, I would like to say a few words about the many Division attorneys and other professionals who worked on this case for the past 13 years. I realize that in many ways this was a thankless task. The trial staff was located in New York, away from day-to-day contact with and support from the rest of the Division. They were litigating against aggressive attorneys, with far better resources and staff support. Nonetheless, the members of the trial staff did their best, against considerable and growing odds, to win the case to which they had been assigned. Their work on the case has clearly reflected their effort and dedication.

Mr. Chairman, this concludes my prepared remarks. I will be glad to address any questions you may have.

U.S. Department of Justice

Antitrust Division

Office of the Assistant Attorney General *Washington, D.C. 20530*

JUN 18 1982

Honorable Strom Thurmond
Chairman, Committee on
The Judiciary
United States Senate
Washington, D.C. 20510

Dear Senator Thurmond:

Enclosed are responses to the questions you submitted under cover letter dated March 23, 1982, regarding the Department's recent settlement agreement with AT&T. In addition, I have enclosed a copy of the Department's response to public comments on the proposed modification which expands on many of the issues raised in your letter of March 23rd. If you have any further questions, please do not hesitate to call upon us.

Sincerely yours,

William F. Baxter
Assistant Attorney General
Antitrust Division

Enclosures

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1. With respect to the extent of market power possessed by AT&T Long Lines, I understand that the Telpak tariff, which provided multiple private lines as a single offering, was withdrawn in 1981, and users were then faced with a 16% private line rate increase and then a 16% general rate increase. Is there any evidence that a significant number of affected subscribers shifted their business away from AT&T? Please provide us with any studies in your possession that quantify the extent of any such shifts.

Answer: We did not examine this question for our case, and made no studies, and could therefore only speculate as to customer shifts occasioned by the cancellation of Telpak.

2. What is AT&T's share of the installed base of terminal equipment in the United States?

Answer: Due to the lack of reliable and comparable data for many types of terminal equipment, it is impossible to state with any certainty AT&T's share of all terminal equipment. According to figures compiled by the North American Telephone Association, in 1980 the Bell System provided 75 percent of the key telephone system capacity in the nation and 69 percent of the private branch exchange (PBX) capacity. Each of these percentages is based on the number of telephone instruments served by the key telephone system or PBX. Those same figures indicate that in 1980 the Bell System provided 81 percent of the nation's telephone instruments.

3. You have expressed the view in the past that commingling of regulated and unregulated activities inevitably raises some concerns about cross-subsidization. Under these circumstances, do you believe that it would be preferable to require some separation between AT&T Long Lines and its competitive activities?

Answer: It is true that the combination of regulated monopoly and competitive activities within a single firm creates both the incentive and opportunity for the cross-subsidization of competitive operations with revenues derived from regulated monopoly operations. The proposed modification will create an industry structure that will deal with this problem. After the divestiture of the regulated local franchise monopolies from AT&T, AT&T Long Lines, while regulated, will be subject increasingly to competition in all of its services. This will constrain AT&T's ability to raise prices above competitive levels in regulated activities in order to subsidize anticompetitive pricing strategies in other markets. Following divestiture, therefore, even though AT&T's intercity services may continue to be regulated, the potential for cross-subsidization will be reduced by competitive forces. In addition, cross-subsidization is often connected with attempts by a dominant firm to engage in predatory pricing by reducing price for a period of time, only to raise price later in the same market when the threat of competition has dissipated. The significant reduction in barriers to entry created by the proposed modification will reduce the incentive to engage in such conduct in the future. It thus appears that any problems arising out of AT&T's dominance in the provision of intercity services will not persist over the long run.

4. What specific costs would be associated with divesting those portions of Western Electric and Bell Labs that develop and manufacture terminal equipment?

Answer: It is not possible for us to provide even an approximate dollar estimate of the "specific costs" that would be associated with the divestiture of the portions of Western Electric and Bell Labs that develop and manufacture terminal equipment. This was not one of the relief options sought by the United States, and no attempt was made to calculate these costs.

5. The settlement requires the transfer of intrastate long distance facilities to AT&T. Presumably, AT&T will thus be designing, constructing, controlling, and administering the

network, while the BOCs still [sic] be limited to providing local access. Do you believe this could create any competitive problems for independent equipment manufacturers by making it more difficult for them to obtain access to network information than it will be for Western Electric to obtain such information?

Answer: The Department believes that the structure of the industry after the required divestiture will encourage an increase in the flow of information to competitive manufacturers. The divested BOCs will control information concerning the provision of local exchange and exchange access service, and will necessarily have access to information concerning the provision of interexchange service necessary to interconnect with the facilities of Long Lines and other interexchange carriers. The Department expects that the divested BOCs will seek out competitive manufacturers and share this technical information with them far more freely once their corporate and financial ties to Western Electric and Bell Laboratories have been severed.

Long Lines itself, moreover, will have incentives to share network information more freely with firms other than Western Electric. As non-discriminatory interconnection of other common carriers by the BOCs fosters competition in the market for interexchange services, Long Lines will experience an increasing need to procure facilities on the basis of quality and price, without regard to corporate affiliation, since to do otherwise would only place it at a competitive disadvantage relative to other interexchange carriers.

6. In your January 25 statement you assert that while Western would have "something of an advantage" because of advanced network information, this advantage is not exploitable because Long Lines would lose market share. Would you please elaborate on this?

Answer: Given the equality of interconnection terms and conditions which will result from the proposed modification, other long distance carriers will become fully competitive with Long Lines. This will significantly dilute Long Lines' market power and share in the markets for long distance services and for purchases of related equipment. Thus any advantage Western might enjoy initially will become less important over time.

In addition, because Long Lines will become subject to competition in its traditionally monopoly services, it will have an incentive to procure equipment in the most efficient manner possible. It will, therefore, have no incentive to procure equipment from Western Electric solely because of its affiliation, since any supra-competitive transfer prices for such equipment would only disadvantage AT&T in the market for intercity services.

7. Do you have any concerns that transferring the embedded terminal equipment to AT&T will give AT&T, in its role as an unregulated terminal equipment vendor, a significant advantage by providing access to detailed customer information such as names and addresses of users, and the type and age of equipment presently installed?

Answer: Although the transfer of embedded Western Electric terminal equipment to AT&T will permit access to certain customer information, the proposed modification will actually reduce AT&T's access to information and eliminate entirely any preferential access to information derived through the provision of monopoly exchange services by the BOCs. AT&T's ownership and control of the Bell operating companies has provided AT&T with a wide range of information regarding all Bell customers of a sort not available to its terminal equipment competitors. The proposed modification will put an end to any competitive advantage AT&T enjoys as a result of its dual status as a provider of both monopoly exchange telecommunications service and terminal equipment. The customer information in AT&T's possession as a result of the transfer of embedded terminal equipment is the same type of information available to any manufacturer concerning its customers. The extent of AT&T's access to such information by virtue of its share of embedded terminal equipment should not be a barrier to competition in this market.

8. What procedures do you believe will help assure that competitors can obtain information about the services and equipment used by AT&T customers in a timely fashion?

Answer: In U.S. v. AT&T, the Department alleged that AT&T withheld technical information required by competitors to provide equipment and services to the BOCs. This was made possible by AT&T's control of virtually the entire network through its ownership of the BOCs. Following divestiture, the BOCs should have an incentive to purchase the least costly, most reliable equipment, and thus an incentive to make their requirements and specifications known to all potential suppliers. In addition, Section II (B)(2) of the proposed modification explicitly prohibits discrimination by the BOCs in the establishment and dissemination of technical information and procurement and interconnection standards.

9. With respect to the types of equipment used to provide long distance telephone service, how much competition currently exists, and are there a significant number of products needed by AT&T Long Lines for which Western Electric is the only current supplier? Besides equipment, what products and services do you expect that Western and Bell Labs will provide to AT&T's long distance operations?

Answer: AT&T Long Lines uses a variety of transmission and switching equipment to provide long distance telephone service. AT&T Long Lines procures its satellite equipment from non-affiliated suppliers. A very high proportion of Long Lines' other long distance transmission equipment is supplied by Western Electric. We do not have precise data showing the proportion of such equipment not readily available from other manufacturers. However, a number of firms currently supply long distance telephone transmission equipment and switching equipment to the non-Bell telephone companies and to the Specialized Common Carriers.

In addition to supplying long distance transmission equipment and switching equipment to AT&T Long Lines, we expect that Bell Labs and Western Electric will continue to supply auxiliary equipment (such as multiplex equipment, protection

switching equipment, alarm and monitoring equipment, and the like) to Long Lines, and that Bell Labs and Western Electric will continue to provide fundamental and network planning to AT&T's long distance operations.

10. Is it expected that Western Electric and Bell Labs will remain intimately involved in the coordination and management of the intercity network? If so, won't this provide funds and network information that give AT&T CPE operations an advantage over independent manufacturers?

Answer: The Department has no reason to believe that Western Electric and Bell Labs will reduce their involvement in the coordination and management of AT&T's portion of the intercity network. The divestiture required by the proposed modification, however, will greatly reduce any anticompetitive advantages AT&T's CPE operations have enjoyed in the past.

The divestiture and equal exchange access required by the modification will subject all of AT&T's services increasingly to competition, and thus greatly reduce, and ultimately eliminate, sources for the cross-subsidization of anticompetitive pricing strategies in competitive markets, including the market for customer premises equipment.

In addition, AT&T's superior access to network information will be greatly diminished with respect to CPE, since the divested BOCs, owners of the facilities to which CPE will be connected, will be the principal repositories of relevant network information. The divested BOCs for the first time will have no incentive to deny such information to non-Western Electric manufacturers.

11. Eric Nelson, Western Electric's Director of Purchasing, is quoted in the January 17 New York Times as saying that Western Electric hopes to sell its purchasing expertise to the Bell Operating Companies. In your view, would the recent settlement permit Western to become the prime purchasing agent for the BOCs? What other products and services do you expect that AT&T will provide to the BOCs?

Answer: The proposed modification would explicitly prohibit Western Electric from becoming the prime purchasing agent for the BOCs. Under Section I(A), AT&T is required to transfer to the BOCs sufficient facilities, personnel, systems, and rights to technical information to perform necessary procurement independently of AT&T. The proposed modification also requires the termination of standard supply contracts between Western Electric and the BOCs. The establishment of Western Electric as the prime purchasing agent for the BOCs would run directly counter to the purpose of the proposed modification, which is to dissolve the vertical relationship between the BOCs and AT&T and Western Electric. The BOCs, of course, in carrying out their procurement functions, are free to purchase any Western Electric products or services consistent with the anti-discrimination provisions of the proposed modification.

With respect to products and services that may be provided by AT&T to the BOCs, Section I(C) of the proposed modification requires that until September 1, 1987, AT&T, Western Electric,

and Bell Labs provide on a priority basis all research, development, manufacturing, and support services necessary to permit the BOCs to fulfill the requirements of the proposed modification. Following divestiture, of course, AT&T, like any other vendor, may provide any product or service to the BOCs that they are willing to buy.

12. Under the proposed settlement, can AT&T refuse to permit the interconnection of non-Western terminal equipment with Western terminal equipment? With AT&T's service offerings? What guarantees are there that AT&T will not restrict interconnection?

Answer: Under the proposed modification, AT&T will have no control over the interconnection of terminal equipment to the network. Interconnection of such equipment to the network, of course, is subject to FCC rules governing interconnection (i.e., the registration program).

13. Roughly how many patents does AT&T have today? How many of them were obtained in the past decade? How many of them pertain to network transmission? To terminal equipment?

Answer: According to records of the United States Patent and Trademark Office, it issued 7,316 patents to AT&T, Bell Laboratories, Western Electric and Teletype Corporation between January 1969 and December 1981. The Patent Office does not maintain records in a form that would permit a ready response to this question for periods prior to 1969. According to AT&T, as of March 1, 1982, it held approximately 9,750 U.S. patents.

Based on the information above, we would estimate that about 6,000 patents were issued to AT&T and its subsidiaries in the past 10 years.

The Department does not have any information which would permit it independently to classify AT&T patents according to type of equipment. According to AT&T, as of March 5, 1982 it had approximately 765 patents which it classified as applicable to transmission facilities and approximately 575 patents which it classified as applicable to terminal equipment.

14. Are you aware of any studies that address the effects of eliminating compulsory licensing, and if so, can you provide them to this Committee?

Answer: We are only aware of one such study, performed by the FCC, which was submitted to the House Subcommittee on Telecommunications, Consumer Protection and Finance on February 26, 1982. We have enclosed a copy of that study with this letter.

15. Did you or your staff consult with Justice Department patent attorneys before completing work on the proposed settlement?

Answer: No Justice Department patent attorneys were consulted while the settlement was being negotiated. In connection with the proposed settlement, however, the principal patent questions concerned existing ownership and licensing patterns, the effects that the settlement might have on them, and the implications of these patterns and effects, if any, on competitive vigor in the industry. These are kinds of issues with which the Division itself regularly deals.

16. Under the proposed settlement, AT&T will retain its control of the network and dominance of the terminal equipment market. If AT&T designs the network or terminal equipment around a patent that it has no obligation to license, do you believe independent manufacturers will be hindered in their ability to manufacture equivalent or compatible equipment?

Answer: Given the assumptions of the question, the answer can only be yes. However, one must consider the likelihood that such a bottleneck patent position could exist. To our knowledge, not since the basic transistor patent has even the potential for such a single controlling patent existed. Indeed, if one technological road is blocked by a patent the result is likely to be to encourage innovation in different directions to avoid the blocking patent. Given the rapid pace of innovation in electronics and related technologies, it seems unlikely that one or even several patents could block competitors for a substantial period of time, especially with respect to terminal equipment.

In the case of network design, it must be remembered that the network now exists. It is not likely to change radically overnight but is more likely to evolve over a lengthy period of time. New technology is introduced gradually and must be compatible with remaining equipment. Again, it seems unlikely that AT&T will be in a position to introduce some dramatically advanced technology into that portion of the network which it controls (particularly because it must interconnect with non-affiliated companies) which would cause its competitors to be unable to continue to provide service.

On both points, however, the problem -- if it is a problem -- derives not from some unique capacity of AT&T to impede competitive development, but from the protections that the patent laws afford in order to stimulate innovation. AT&T is, indeed, a strong contributor to technological development, but many other firms are as well. The proposed settlement, by eliminating the arrangements by which local monopoly revenues funded AT&T research, will cause AT&T to compete with other firms, in this and other areas, on equal grounds.

17. Your competitive impact statement states, "there appears to be no reason for AT&T to refuse to continue to grant licenses under existing patents." On what information did you base this conclusion?

Answer: There are several factors which lead us to believe that the quoted statement is accurate. AT&T began its extensive patent licensing program before the entry of the 1956 consent decree. Indeed, it has published annual offers in the U.S. Patent Office Official Gazette since about 1949 to license others for any purpose at reasonable royalties. Many of AT&T's existing patents are already licensed to its competitors for the life of the patents with a five-year new invention clause. Given the number of outstanding licenses and licensed competitors, there would appear to be no incentive for AT&T to refuse to license new competitors as well. In addition, electronics and telecommunications technology has progressed rapidly with a large number of firms involved in research and development and has yielded substantial patent positions for a number of such firms. Thus, there will be significant incentives and benefits for AT&T to license its patents in order to obtain access to the patents of others.

18. The proposed settlement does not include Cincinnati Bell Inc. and Southern New England Telephone Company in the list of Bell Operating Companies. If AT&T can consolidate its control of SNET and CBI and can buy other local exchange companies, won't this perpetuate the same problems that the proposed settlement is intended to eliminate?

Answer: Under Section I(D) of the proposed modification, AT&T is prohibited from reacquiring the stock or assets of a divested BOC. This provision, therefore, precludes the reestablishment of the same vertical relationships the modification was designed to end. While the modification does not prohibit the acquisition of a local exchange company other than a divested BOC, any such acquisition would be subject to scrutiny by the FCC under §221 of the Communications Act or by the Department of Justice under the Clayton Act. The Department, of course, would look with disfavor on any arrangement which would threaten to re-create an anticompetitive market structure.

19. Customer-premise wiring brings the Bell Operating Companies' service to the customer's equipment. Since existing wiring cannot be economically replicated, it would seem to be a bottleneck facility just as is the local loop. Representatives of AT&T and the Justice Department have testified that such wiring will remain in the control of the Bell Operating Companies, rather than being transferred to AT&T, but this is not clear on the face of the settlement. Will the proposed settlement be clarified with respect to the treatment of customer-premises wiring?

Answer: As the question notes, both the Department and AT&T are of the view that the proposed modification places the provision and maintenance of inside wiring within the control of the BOCs. In light of this agreement there appears to be no reason to seek any clarifying change in the proposed modification.

20. Since the BOCs will be restricted to the provision of access lines or access service from the customer premises of AT&T's switching locations for connection to AT&T's interexchange services, will decisions as to which equipment will be located on the customers' premises and connected to such services be made by AT&T or by the BOCs? Will it be AT&T or the BOCs that provides any telephone company-provided equipment at the customers' premises for connection to the access lines? To AT&T's services?

Answer: Under the terms of the proposed modification the BOCs would be prohibited from the manufacture or provision of telecommunications products or customer premises equipment except for emergency services. Customer premises equipment is defined as equipment employed on the premises of a person (other than a carrier) to originate, route, or terminate telecommunications, but does not include equipment used to multiplex, maintain, or terminate access lines.

Therefore, AT&T and not the BOCs will provide CPE and telecommunications products which are connected to either BOC access lines or directly to AT&T services, and any decisions regarding the location of such equipment or products at a customer's premises would have to be made by AT&T and, of course, the customer involved. The BOCs would provide only that equipment used to multiplex, maintain, or terminate access lines.

21. Will the BOCs be participating with AT&T in the provision of joint services (where the BOCs provide the local access) or will they merely be providing access to those AT&T-provided services? Will independent telephone companies cease to provide joint services and instead provide access service? What will be the consequences of such a change for the provision of customer-premises equipment?

Answer: Under Appendix B to the proposed modification the BOCs are required to file tariffs for exchange access which will replace the current division of revenues process. The appendix also provides that each BOC offering exchange access as a part of a joint or through service must make exchange access available to all interexchange carriers on the same terms and conditions. This latter provision recognizes that there may be instances in which regulatory statutes may imply that a BOC is engaged in the provision of a joint or through service, such as where a BOC provides billing services. Regardless of whether, under relevant regulatory statutes, a BOC is regarded as providing a joint or through service, the modification provides that the sole mechanism for compensating the BOC shall be through access charge tariffs available to all interexchange carriers on equal terms and conditions. The replacement of the division of revenue process with access charge tariffs applies, under the terms of the modification, only to exchange access provided by BOCs, and therefore does not directly affect the settlements process between independent telephone companies and AT&T.

It is not apparent that the substitution of access charge tariffs for the division of revenue process will have any direct effect on the provision of customer premises equipment. Deregulation of such equipment under the FCC's Second Computer Inquiry decision, of course, will have an effect on the computation of jurisdictional separations.

AFTERNOON SESSION

Senator SPECTER. It is now 2:30, the time set for the reconvening of the hearings on oversight of recent actions of the Department of Justice in *U.S.* v. *AT&T.*

This afternoon we have Mr. Morris Tanenbaum, executive vice president of AT&T, and Howard J. Trienens, vice president and general counsel of AT&T.

Mr. Tanenbaum, we shall begin with you. The custom of the committee is to request that statements be summarized, leaving the maximum time available for questioning.

TESTIMONY OF MORRIS TANENBAUM, EXECUTIVE VICE PRESIDENT, AT&T, NEW YORK, N.Y.

Mr. TANENBAUM. Thank you, Senator.

I am Morris Tanenbaum and this is Mr. Trienens. We welcome the opportunity to appear before you in order to discuss the agreement that we have reached with the U.S. Department of Justice which modifies the 1956 consent decree. We will be pleased to respond to any questions that you might have.

Senator SPECTER. Mr. Tanenbaum, as a matter of procedure I think we might interrupt you at this point to swear you in in the absence of Chairman Thurmond. He did not do that at the start of the hearing, did he?

Mr. TANENBAUM. No, he did not.

Senator SPECTER. Raise your right hand. Do you swear that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth, so help you God?

Mr. TANENBAUM. I do.

Senator SPECTER. You may proceed, Mr. Tanenbaum.

Mr. TANENBAUM. I will address the 1982 decree, including a brief description of it and the reasons for its negotiation. I will then talk about the impact of this action, after which Mr. Trienens will discuss the procedures used in filing the decree and its current status.

For the reasons that Professor Baxter mentioned and on which I will expand in just a moment, the 1982 consent decree is proposed as a modification of the 1956 decree. Under the terms of the modified decree, AT&T will divest the local exchange operations of 22 Bell operating companies. These facilities represent about two-thirds of the Bell System's total plant or over $80 billion in assets.

The divested local exchange companies are required to provide equal access to their local services to all interexchange carriers and information service providers under terms virtually identical to those that are contained in S. 898.

All the Bell System interstate long-distance facilities and a portion of the intrastate long-distance facilities now owned by the Bell operating companies will remain part of AT&T. Ownership of customer premises equipment will also be retained by AT&T along with Western Electric and Bell Laboratories.

Of the Bell System's approximately 1 million employees, about one-half will work for the new local exchange companies upon divestiture while the other half will work for AT&T and the units that remain with it.

According to the modified decree, the divestiture will take place within 18 months of its acceptance. A plan for reorganizing to accommodate this divestiture must be filed with the Department of Justice within 6 months of the effective date of the modified decree.

Termination of the 1956 consent decree, which is a cornerstone of the agreement to divest the local exchange operations, removes restrictions imposed by that decree on AT&T. This action, along with preserving Bell Laboratories and Western Electric as integral parts of AT&T, technologically integrated with the Bell System's part of the nationwide network, is a key element, we believe, in maintaining America's world leadership in the information age and the technology upon which that leadership is based.

The benefits derived through replacing the 1956 decree with a new decree will enhance the competitive viability of the Bell System in overseas markets, which has obvious benefits with respect to the U.S. balance of trade.

Perhaps the question we are most frequently asked is why did we agree to this decree. Why after years of contesting any change in the structure of the Bell System as threatening to the cost and quality of telephone service in the United States have we suddenly consented to a major divestiture of just the kind that we so vigorously resisted and about which I testified before this committee just last year?

The answer to that question requires a bit of historical perspective. First of all, the divestiture is not our idea. Many generations of management of the Bell System including the current one have believed that the best way to provide telephone service is through an organization that is highly integrated both horizontally and technologically. We pointed to the uncontested fact that this country has the best telephone system in the world as evidence of that.

We continue to believe that in the highly regulated single supplier—monopoly, if you will—environment that characterized the industry well into the 1960's, a single highly integrated structure is the best way to provide the highest quality, lowest cost telephone service.

However, slowly—indeed, I might say painfully—over the last decade or so it has become clear that the environment has changed and continues to change rapidly. Under the force of new technology which blurs the distinction between telephone service and other functions, notably data processing, with the achievement of universal service at very low cost, and with the growing importance of telecommunications to the total society as we enter the information age, the consumer is no longer satisfied with a single supplier.

Variety, convenience, and choice, driven by competition, is what the public is demanding. That demand is reflected in the actions of the public's representatives, the Congress, the regulators, and the courts.

Slowly and painfully the management of the Bell System began to realize that the structure which served so well in the old environment would not serve well in the new if the Bell System was to continue to participate and innovate in the new world of communications and the information age.

Thus what has been going on intensively for a decade is the search for accommodations that will preserve the most important values of the old structure but that would be acceptable to the public with its concern about fair competition, open markets, and no cross-subsidies.

The first solution was the separate subsidiary mandated in the FCC's second computer inquiry. We accepted that. As the Congress became interested in the industry, more complete separation, including a split in the research and development and manufacturing functions, was mandated along with market tests and purchasing quotas. Legislation was introduced in the House calling for other forms of quasi-separation such as requiring divestiture of a portion of the unregulated subsidiary.

Overhanging all this was the deepening shadow of the 1956 consent decree which substantially restricted the ability of AT&T to take full advantage of our own technology in the data processing impacted world of telecommunications and expanding opportunities of solid state electronics. Increasingly, it became apparent that the old structure which has served so well would not be viable in the New World. A major change was necessary.

The modified consent decree is such a change. By divesting the local exchange companies, it eliminates the concerns of cross-subsidy from a monopoly operation. It breaks the perceived bottleneck of access for all intercity carriers. At the same time, the decree maintains the integrity of the Bell nationwide intercity network and preserves the technological integration of that network with Bell Labs and Western Electric. While highly competitive, this network still provides the basic infrastructure of the Nation's telephone system and the glue which ties the nationwide system together.

The preservation of the Bell Labs' relationship with Western Electric and the intercity network will provide the conditions necessary for continued innovation and international leadership in telecommunications technology. The modified decree removes the shadows of the 1956 decree and the anticipated years of litigation and uncertainty associated with the 1974 antitrust case.

Thus, while the decree is not the result we had originally desired and anticipated, we concluded it is the best solution available in the current climate. It will enable the industry to move forward in the directions toward which the regulators and the Congress have been urging us.

Now let me turn to the impact of the modified decree. The concern was expressed several times this morning about effects on local rates. Let me just confirm what Mr. Baxter said. The upward pressure on local telephone rates that we have been talking about for years and that has been so prominently featured in discussions recently is not a result of the modified decree. It is a result of today's competitive environment and of inflation.

The Bell System has a long successful history of holding down the costs of its services to the Nation's telecommunication users. In 1941 it required about 6 hours of wages of the average manufacturing employee to pay for 1 month's telephone service. By 1971 that had dropped to 1 hour 48 minutes. It is now a little less than 1¼ hours.

Over the last decade, records of many hearings relating to the growth of competition in the telecommunications industry have pointed to one inevitable outcome: Rates for all services will be driven to a relationship closer to their costs. This when combined with inflation as a fact of life inevitably means upward pressure on local rates. However, I do wish to underscore that this upward pressure on local rates is not a consequence of the divestiture agreement.

How about the quality of service? The Bell System remains committed to the best possible service at the lowest possible cost. The companies which will be divested will start their new life in a financially strong position so that they can meet this commitment in the future.

Accordingly, the decree requires AT&T to assure that upon divestiture the local exchange companies have sufficient personnel, sufficient facilities, and rights to technical information which will permit them to perform their functions. In addition, for a 5-year transition period, AT&T, Western Electric, and Bell Laboratories will provide on a priority basis the manufacturing, research, and development services that the local exchange companies will need to fulfill their requirements under the decree.

With established customer acceptance, a strong balance sheet, strong revenue streams from local service and from access charges, full freedom to apply technology, and the continued oversight of State regulatory bodies, the commitment to the best possible service at the lowest possible cost should continue undiminished in these new companies. That same commitment will apply to the services that are supplied by the remaining AT&T.

Another area of concern has been the impact on national security, national defense, and emergency preparedness. The modified decree preserves the unified management of the nationwide public long-distance network. By mandating a central point of coordination in the local exchange companies it takes explicit account of national defense and emergency preparedness. As details of the divestiture develop, these national concerns will continue to be addressed. We will of course cooperate fully with the Department of Defense and all other agencies of the Federal Government which have responsibilities in these areas.

How about employees? Senator Metzenbaum in particular raised those questions. The modified decree does not change benefits, including pensions for active or retired Bell System employees. Nor will the decree alter any existing bargaining agreements covering Bell employees. We believe employees will benefit from the resolution of much of the uncertainty which has affected their jobs over the last few years. They will also benefit over the long run as they are employed by financially sound viable entities in their respective businesses.

We also of course have a responsibility to our shareowners, most of whom are small investors holding less than 100 shares which often represent an important part of their life savings. After the divestiture of the local exchange companies shareowners will retain the full interest in the assets that currently comprise their investment.

The only difference is that their investment will be divided in stock in the remaining AT&T and a proportionate interest in the local exchange companies that will in the future operate separately from AT&T. Shareowners will also benefit from the operation of financially and operationally viable entities in an environment of reduced uncertainty.

Senator, we believe the modified decree is in the public interest. It removes the anticompetitive restrictions applied to the Bell System that were the result of an era of pervasive public utility regulation in a monopoly marketplace. Moreover, it tracks closely the goals contained in S. 898 as approved by the Senate last October.

Now I might ask Mr. Trienens to make his statement, or would you prefer to raise questions now?

Senator SPECTER. I think that would be fine if Mr. Trienens proceeded at this time.

Mr. Trienens, if you will stand, I will administer the oath.

Do you swear that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth, so help you God?

Mr. TRIENENS. I do.

Senator SPECTER. You may proceed.

TESTIMONY OF HOWARD J. TRIENENS, VICE PRESIDENT AND GENERAL COUNSEL, AT&T, NEW YORK, N.Y.

Mr. TRIENENS. My statement is basically a presentation to the committee of the court papers that have been filed on January 8 and subsequently. It took a little less than 2 weeks to straighten out the procedures so that the two cases were before one judge for a Tunney Act type proceeding in which every comma of the Tunney Act procedures will be applied.

That was the purpose at the outset, as shown by the court papers that were filed. The purpose has been achieved. It was necessarily complex because the principal virtue of this settlement from our point of view was ridding ourselves of what we regarded as the archaic restraints and increasingly restrictive restraints of the 1956 decree.

We had to deal with that case. It was considered desirable to have it all heard in one hearing before Judge Greene. In somewhat less than 2 weeks that has all been accomplished. It is now underway. We have every confidence that upon the completion of those hearings the modified decree will be found to have been in the public interest and will be entered.

Thank you.

Senator SPECTER. Senator Thurmond, the chairman of the Committee on the Judiciary, could not be present this afternoon as he announced this morning. He asked that a series of questions be directed to you gentlemen, which I shall do at this moment.

First, Senator Thurmond wanted to ask the same question asked of Mr. Baxter regarding the effect of this proposed modification of the consent decree on the rates that consumers, particularly in rural areas, will have to pay for local telephone service. Do you expect those rates to increase substantially?

Mr. TANENBAUM. As I have mentioned in my oral statement and in my filed statement, the pressure on those rates, the upward pressure on local rates in total, results from factors completely separate from this modification of the 1956 decree. We do not believe that the modification of the decree will in any significant way affect those rates. What actually happens to those rates will continue to remain completely in the hands of the regulatory authorities.

Senator SPECTER. Are you saying, Mr. Tanenbaum, that in your judgment there will be no increase at all in rates which would be attributable to this divestiture?

Mr. TANENBAUM. Not by this decree itself, nothing significant.

Senator SPECTER. At the present time are local rates in effect subsidized by other aspects of profits of AT&T?

Mr. TANENBAUM. In our opinion, local rates receive substantial subsidy from long distance rates due to the way costs are allocated for the use of common facilities. This decree provides a mechanism in the hands of the regulatory authorities to continue those subsidies at whatever level they wish.

Senator SPECTER. Would it be your expectation then that the mechanisms which were described this morning by Mr. Baxter would be utilized by the local PUC's to extract the same kind of subsidies from connection charges for long distance from AT&T which will now be a separate entity?

Mr. TANENBAUM. It is my belief that those mechanisms are there. They have been used in the past for this purpose. It is my belief that between them the State regulators and of course the FCC, which does have jurisdiction over interstate communications, will arrive at what they believe in their best judgment and within their authority is the proper way to handle that matter. I have no reason to believe that they will perceive that any differently in the future than they have in the past.

Senator SPECTER. Mr. Tanenbaum, the question is will AT&T be objecting to having those same kinds of subsidies paid when AT&T is separate from the local operating company, or will AT&T come into those proceedings before the local PUC's or the FCC and say, "We understand there has been this tradition for subsidy. We paid these subsidies when the local operating company—for example, Bell of Pennsylvania to just pick a company at random—were in effect in the past through a variety of ways that we operated: the Yellow Pages, long distance rates, the series of fund flows, Western Electric. We understood when the divestiture occurred that we would be continuing in one procedural way or another to pay those subsidies. We are willing to have that same rate, except for inflation which we think has to be added on to the consumer. We are prepared to have those same subsidies charged through these indirect methods which have been eloquently stated by Professor Baxter in that old testimony back on January 25 before the Senate Judiciary Committee?'

Mr. TANENBAUM. Senator, first of all, let me say that it is more than just AT&T that is involved here because those access charges will be paid by everyone providing interexchange telecommunication services. Our position has been for several years now—I do not see it changing—that we understand the need for that subsidy, but we really believe that with competition in this area those rates are

going to have to be moved down toward the actual costs of providing those services.

Senator SPECTER. You do not mean down to, you mean up to.

Mr. TANENBAUM. The long distance rates will have to be driven down to the cost of providing the long distance services.

Senator SPECTER. Are you saying then that AT&T will not be able to pay the same kinds of subsidies that it has allocated in the past to local rates?

Mr. TANENBAUM. I do not believe that anybody in this business, not just AT&T but anybody in this business of providing what we call message telecommunication service, the long distance toll service, will be able to pay rates that are substantially above the costs of providing those services for any length of time because there are so many private parties that will be able to bypass those services if they are artifically priced too high, if they are artificially priced above the cost of providing them.

Senator SPECTER. Is a consequence of what you just testified to that AT&T will not have moneys from the long distance profits to continue to subsidize local rates as they have up to this point?

Mr. TANENBAUM. AT&T will be paying a substantial portion of those revenues as access charges and does indeed expect to continue to make a reasonable return on those services. That return of course is currently regulated by the FCC.

What I am really saying is that if those long distance rates are artifically held high by any mechanism—by high, I mean well above their costs—other parties will find ways to bypass those services and not pay those high costs.

Senator SPECTER. Mr. Tanenbaum, we are not talking about keeping the rates up. So far as the consumers in Pennsylvania are concerned on local telephone service, they do not care what the rates are on long distance charges. All they care about is the subsidy rate.

Mr. TANENBAUM. Senator, the citizens of Pennsylvania I am sure use long distance service. The rates of long distance service must be of concern to them just as the rates of their local service are of concern to them.

Senator SPECTER. I was focusing just for the moment on the local rates. The question that I am putting to you turns on what the local rates will be compared to what they are now considering what the subsidies are at the present time with the unified system contrasted to what the subsidies will be with a divested system. That is what I am concerned about.

Mr. TANENBAUM. Let me try to address that as clearly as I can. I will try to understand your question.

Our belief has been for many years now—ever since competition was first introduced into this telephone business—that with competition you cannot maintain cross subsidies. If you cannot maintain cross subsidies, then that means the rates on both sides will have to approximate their costs. The local rates will have to approximate their costs and the long distance costs will have to approximate their costs.

What that says is that since the cross subsidy has been flowing from long distance to local rates, those local rates will have to go up and the long distance rates will not go up nearly as fast. In fact,

if inflation is low enough, they will actually come down. Both of those will end up at prices that are much more closely associated with the real cost of providing them.

Senator SPECTER. What is your best estimate then as to how much local telephone rates will go up?

Mr. TANENBAUM. There has been a lot of talk about that. A great deal depends on the assumptions that you make. Let me give you one set of assumptions and what that would result in.

With inflation at about a 10-percent rate—we have managed to offset about half of that through very high productivity—and if we were to bring this cross subsidy from where it is today down to a level based on the actual usage of those facilities—now it is about three times higher than it would be if you based it just on how much those local facilities are used for long distance—if you did that over a 10-year period, assuming everything else stayed about the same—the economy kept growing about the way it is and everything else that you have to assume in an economic situation—then local rates would tend to go up at about some place in the neighborhood of 8 to 10 percent per year over the next 5 years.

That means if the average rate is about $10 a month now, that monthly rate would go up a little less than a dollar per year for the next 5 years.

Senator SPECTER. Then you are saying that the local telephone rates will go up to reflect inflation but only inflation.

Mr. TANENBAUM. No. I made an assumption of 10 percent for inflation. I also assumed that you take this cross subsidy that currently exists from long distance to local. You reduce that over a period of 10 years so that you bring that down from its current level, which is about 3.3 times. Let me just explain that for a second.

The real problem, as I think Professor Baxter tried to point out, is the question of how you allocate the costs of those local facilities that are used both for local service and long distance service. How should you allocate those costs?

It is our belief that they ought to be allocated at most on the basis of how they are used. If they are used x percent of the time for long distance, then x percent of that cost ought to be charged for long distance.

At the present time about 330 percent more than that usage factor is charged to long distance. If you bring that from that 330 percent factor down to a level based upon the way they are actually used—you do that over a 10-year period of time—and if inflation is also going up at 10 percent a year, then the net overall effect of those two factors would be to increase local rates in the neighborhood of 8 to 10 percent a year.

Senator SPECTER. How do you increase it 8 to 10 percent a year if you are calculating the inflation rate at 10 percent?

Mr. TANENBAUM. Because we offset about half that inflation rate through higher productivity. By the inflation rate I mean the consumer price index. We have typically offset the consumer price index by about 5 percent per year for dozens of years.

Senator SPECTER. Because of higher productivity?

Mr. TANENBAUM. That is right.

Senator SPECTER. When you talk about a figure of 330 percent, what does that mean in terms of the amount of the subsidy? This morning I asked Mr. Baxter the question about what was the amount of the subsidy as nearly as he could state it. You were here and heard him say he did not know. We said we would direct the question to you. Can you shed some light on the question as to what is the amount of the subsidy?

Mr. TANENBAUM. Let me try. About 36 or 37 cents out of every dollar that you pay for a long distance call goes to cover the costs of the use of those local facilities. That is what we call the nontraffic sensitive plant that Professor Baxter referred to. That is your telephone, all your wires, and all the things that have to be there whether you use it or not.

If that were based on just the percentage of usage, that number would be cut down by a factor of about 3.3 or 330 percent. The total number of dollars——

Senator SPECTER. You are saying it would be about 10 cents.

Mr. TANENBAUM. That is right. It is in the neighborhood of 10 to 12 cents.

Senator SPECTER. If it is reduced, say, to 12 cents from 36 cents, that is a 24 cent drop over 10 years.

Mr. TANENBAUM. That is right.

Senator SPECTER. How does that figure relate in a percentage way to the cost of telephone service?

Mr. TANENBAUM. As I said, that plus inflation would result over the next 5 years to about 8 to 10 percent a year. About half of that is inflation. The other half is due to that fact, plus other facts of increased depreciation rates that are approved or pending again due to the speed of technology and competition.

There are a number of factors that get into that, but the number that I would suggest is the easiest one to keep in mind is, of this 8 to 10 percent a year, about half of that is due to inflation. The other half is due to what I suggest is primarily competition which forces costs to rise and which forces depreciation rates down to the actual experience life of the equipment. Those factors together would amount to about four or five percent per year.

Senator SPECTER. I do not understand yet how much of that 8 to 10 percent is occasioned by a change in the amount that the charge is allocated for long distance to that equipment.

Mr. TANENBAUM. I would have to ask your permission to give you a better analysis of that because I do not at the moment have that separation between the long distance subsidy we are talking about and a number of other factors that are happening, primarily faster depreciation rates. Those together are about 4 or 5 percent, about half of that.

Senator SPECTER. Let me proceed to the balance of Senator Thurmond's questions. Then I want to come back to this.

Mr. TRIENENS. May I interject one point on this?

Senator SPECTER. Yes, of course. Mr. Trienens, please feel free. I do not intend to ask you these questions separately. If you have anything to add as I go through Senator Thurmond's questions, please do so. When we come to my questions, I will ask you specifically. However, he wants both you and Mr. Tanenbaum to respond to these questions.

Mr. TRIENENS. I appreciate that very much.

The point I want to make is that there is now pending before the FCC a recommendation of a joint board made up of State and Federal regulators that last year began to face up to the problem Dr. Tanenbaum is talking about of how you deal with this shift of the burden of the nontraffic sensitive plant.

Senator SPECTER. The burden of what?

Mr. TRIENENS. Of the allocation of the costs of the nontraffic sensitive plant. This 3.3 factor has been so——

Senator SPECTER. The allocation of the costs of what?

Mr. TRIENENS. Of the nontraffic sensitive plant as between the interstate and intrastate. That formula which Mr. Tanenbaum speaks of is prescribed in a rule of the FCC. A joint board made of State and Federal regulators has recommended a change in that that would in effect alter in a degree and in a transition the amount of that 3.3 allocation, which we believe has to be made when driven by forces of competition.

The reason I point out that this was done last year is that these forces are going on and are being dealt with totally independent of this divestiture restructure of the Bell System. These amounts of rate increases in the magnitude of eight percent a year as compared with the 4 percent in bygone days has also been happening and indeed did occur in 1981.

These things were on the way and were being dealt with and had already had their impact somewhat felt before anybody ever addressed the question of the divestiture decree. That is the point Professor Baxter was making that the decree is essentially irrelevant to the very serious but the very different problem that we are now discussing.

Senator SPECTER. We shall come back to that.

Second, Senator Thurmond would like you to clarify how you see the Tunney requirements as applicable to this proposed modification and whether you think they should apply to the plan of reorganization as well.

Mr. TRIENENS. As to the application of the Tunney Act procedures—I mean all of them—to this proposed modification of the consent decree, it was our proposal from the outset and it has been accomplished that they be applied to this modification.

The reason is that my client does not have any particular interest in all these other old decrees. We are only worried about the one. The one thing we cannot afford to have is a great deal of legal uncertainty, a procedure that does not comply with the Tunney Act, and then a lot of appeals as to whether the Tunney Act should or should not apply. We cannot afford that uncertainty. We cannot afford to have this transition period which makes interim financing very difficult last any longer than it has to.

Therefore, we were very much insistent that these Tunney Act procedures be applied. It seemed sensible to apply them right here in Washington. That has been achieved.

Could you remind me what the last part of that question was? There was a different twist on the last half of it.

Senator SPECTER. Whether you think they should apply to the plan of reorganization as well.

Mr. TRIENENS. The answer to that is no. I think there is some misunderstanding as though that has some separate terrific problem to it. The essence of the separation that is required here, the one thing that Professor Baxter wanted, is the separation between the local exchange network operation from everything else which is either regulated competitive or unregulated competitive. That separation is the key to it. The definitions that are in the decree itself are the key to how that is provided.

The really only exciting and provocative thing to talk about is how many companies, 1 or 49, and how their capital structure is set up. That is one which really follows to some degree. Once you have decided the allocation of the separate local exchange from others, a lot of it is mechanical.

The decision about 1 and 49 is not mechanical, but it is one where we do not expect one. I think you will find this is going to be a very unexciting subject. It is one that is largely mechanical and one that really does not need a whole new round of comment and due process of the detail provided in the Tunney Act.

Mr. Baxter says he is going to have public comment on it, but it should not and cannot take this much time to go through that again because, to repeat, the company cannot afford to have this period in which interim financing is very difficult to extend very long.

Senator SPECTER. Mr. Trienens, if the Tunney Act applies, it applies to the entire subject matter, does it not?

Mr. TRIENENS. It applies to the modified decree and whether that decree as written is in the public interest.

Senator SPECTER. However, the modified decree says that a proposal is going to be submitted by AT&T in 6 months and that proposal is going to be submitted to the Justice Department.

Mr. TRIENENS. That is a purely mechanical application of the standards of the decree itself. The standards of the decree, what it mandates, the separation it dictates, there is a question as to whether those are in the public interest, and, indeed, whether it is appropriate to leave anything to AT&T. The decree does leave some things to AT&T to decide. Whether that is in the public interest to leave it to AT&T to decide is a matter for Judge Greene.

Senator SPECTER. If it should come up that AT&T recommends one company to operate all of the 22 local telephone systems, would you say that would be a purely mechanical conclusion?

Mr. TRIENENS. I say two things about that. In the first place, I think I can assure you it is not going to be one. It is not our intention to have one.

Senator SPECTER. I do not really focus on whether it is one or not. I am focusing on the issue of who is to decide it. When you put the label mechanical on it, you are saying that it does not require court supervision. However, if AT&T has the power to have it one and say it is not up to the court, then it removes it from the court and leaves it to AT&T subject to Department of Justice acquiescence.

Mr. TRIENENS. If the decree standard which requires this separation—which makes pretty much irrelevant whether there is one or not for all the reasons Professor Baxter stated—if the decree which gives that latitude to AT&T is not in the public interest, Judge

Greene presumably would so find. I would hope he would listen to the reasons Professor Baxter gave as to why given the separation, which is the key to this thing, the separation of ownership between the local exchange so-called bottleneck and the rest, does not make any difference. I would hope Judge Greene would listen to that.

However, if he is concerned that allowing that latitude to AT&T renders the decree not in the public interest, he would so find. I would hope he would not.

Senator SPECTER. The third question Senator Thurmond has is: For years AT&T has taken the position that an integrated network was vital to keep providing low cost, high quality telephone service to the consumer. From this standpoint, would it not have been better to retain the Bell operating companies and divest Western Electric instead?

Mr. TANENBAUM. I tried to address that in my oral comments, but let me address it again. We have stated that it is at least as important—in fact, in our opinion more important—that we maintain the technological integration brought about by Bell Laboratories and Western Electric working with the operating part of the telephone company. Clearly our decision on this decree is a reflection of our feeling that it is even more important to retain that in conjunction with the long distance. If we have to make that break, then that break is best made with the local operating part of the telephone companies.

They will still have available to them the technology from Western Electric and Bell Laboratories and the technology from every other supplier in the country and in fact the world because they represent a very large market for sophisticated telecommunications equipment, but that was the decision we had to make in order to achieve what this decree achieves.

Senator SPECTER. When you say they will have that available to them, are you suggesting that it would not be better available when AT&T was one integrated system?

Mr. TANENBAUM. I think it would be much better if AT&T and the Bell operating companies and the long distance companies and the Western Electric Co. and the Bell Laboratories and all of that were together fully integrated, fully able to operate in all areas of telecommunications without restrictions and bars such as the 1956 consent decree and the barriers that the FCC has found it necessary to erect and that the Congress has been seriously considering. I think that would be a very much better scenario.

However, we have concluded that, with the determination to introduce competition into this business that occurred over a decade ago and that has been growing and with what the regulators have concluded and what the Congress has been seriously discussing are necessary barriers to erect and requirements to impose to permit that to happen, that wonderful world that we had and that built this Nation's great telephone system was no longer possible. That is what has led us to this determination.

Senator SPECTER. Senator Thurmond's fourth question is: Do you know if there is any preference within AT&T as to how the BOC's should be organized after divestiture?

Mr. TRIENENS. I think the response I made earlier that it is not our present expectation that there will be one company would be

responsive to that. Precisely how to configure them so that they are ecomically viable and can finance themselves is still under very serious study.

Senator SPECTER. Senator Thurmond's fifth question: What instructions, if any, has AT&T given to the Bell operating companies in commenting on the recent settlement?

Mr. TANENBAUM. We have thoroughly explored that settlement and the possibility of it with the head officers of the Bell operating companies before we went ahead with it. We have met with them since then. We expect to be meeting with them regularly. They will be very much involved and very much a part of helping us reach this decision as to how they should be structured.

Senator SPECTER. Senator Thurmond's sixth question: There have been reports that AT&T is circulating a 90-page document which explains AT&T's understanding of the settlement provisions in some detail. Will you provide this committee with a copy of that document?

Mr. TANENBAUM. I am sorry, Senator. I do not recognize that document.

Senator SPECTER. Is there any such 90-page document that explains AT&T's understanding of the settlement provisions?

Mr. TANENBAUM. Not that I recognize. We of course have prepared a lot of information primarily for the press and others. Our understanding of the decree has been made publicly available.

Senator SPECTER. Is there any substantial document other than that which has already been provided to the press which explains AT&T's understanding of the settlement provisions?

Mr. TANENBAUM. I am not aware of anything that is not fully covered in what we have released.

Mr. TRIENENS. Nor am I.

Senator SPECTER. Mr. Trienens, you say you are not either?

Mr. TRIENENS. No.

Senator SPECTER. Senator Thurmond's seventh question: Do you think that the interests of the BOC's as separate entities can be adequately represented without having a separate representation in the court proceeding?

Mr. TRIENENS. The answer to that is, yes, sir. The duty of the chairman of the board and chief executive of AT&T is to look after all the stockholders. The stockholders have a 65- to 70-percent interest. Seventy percent of their investment is in these local operating companies. He has to act in the best interests of the stockholders as a whole. He would be shooting them and himself in the foot if he were to cast them out in any way other than fully viable companies.

There is no conflict of interest. I see no reason to clutter this up with any controversy or independent counsel or other mechanisms that would simply cause more litigation and more confusion in a period when we have to do this job and we have to minimize the interim financing problems we have to get this job done. We cannot take very long with this.

Mr. TANENBAUM. In addition to the responsibility to our shareholders which we feel very heavily, we also have in the future AT&T in our enlightened self-interests the need for those compa-

nies to be healthy and viable. We are going to be depending on them in order to complete any telephone calls anywhere.

Senator SPECTER. Senator Thurmond's eighth question: Does AT&T still intend to establish a separate subsidiary to conduct its unregulated activities? If so, will it perform its own research, development, and manufacturing?

Mr. TANENBAUM. We fully intend to continue to move ahead, as we are required by Computer Inquiry II, to establish a separate subsidiary to provide the customer premise equipment and enhanced services. CI–II does not require separating the Western Electric Co., the manfacturing facilities, or the research and development facilities. We do not think that is necessary or appropriate. The FCC apparently also feels similarly about that.

We also believe that this decree so substantially restructures the AT&T Co., as well as the effect on the industry at large, and so completely removes any possibility for the kind of cross-subsidies that were of the concern that led to the requirement for separate subsidiaries in the first place, and now puts AT&T very much in the same position as many of our competitors—very large companies, fully integrated without any restrictions or separate subsidiary requirements or what have you—that we believe that whatever is required should be required of anyone in this business and there should be no special requirements just upon AT&T.

Senator SPECTER. Mr. Tanenbaum, I would like to go back to question five to get a specific answer from you. As I give these questions, I would expect you gentlemen to answer them fully. If there is any disagreement with the preceding answer or anything to supplement, please come forward at that time rather than having them repeated.

Mr. Tanenbaum, I would like your specific response to the question concerning what instructions, if any, has AT&T given to the Bell operating companies in commenting on the recent settlement?

Mr. TANENBAUM. Would you say that again? Instructions on what?

Senator SPECTER. What instructions, if any, has AT&T given to the Bell operating companies in commenting on the recent settlement?

Mr. TANENBAUM. We have not given them any instructions in commenting on the recent settlement. We provided them with all the information that anyone else is provided. When we have seen anything that to us looked like it was being misinterpreted, we have informed them of comments that may have appeared in the press or elsewhere that they might want to comment on to straighten out.

Senator SPECTER. There has been no limitation by AT&T in saying to any of the Bell operating companies, "Do not make a comment."

Mr. TANENBAUM. Nothing that I am aware of.

Senator SPECTER. If they felt they wanted to make a comment, given the corporate organization, they could have done so?

Mr. TANENBAUM. Absolutely.

Senator SPECTER. Did you raise your hand, Mr. Trienens?

Mr. TRIENENS. No. That is absolutely correct.

Senator SPECTER. I suppose they would be somewhat reluctant to, though given the realities of corporate life. They are all part of the AT&T chain and all subordinate to the AT&T board of directors and executive management, are they not?

Mr. TRIENENS. They are all part of the Bell System. That is correct.

Senator SPECTER. Therefore they are all subordinate to the instructions, for example, of Mr. Tanenbaum in his position as executive vice president.

Mr. TANENBAUM. They have their own boards and they are responsible to their own boards as well. They are responsible to their own people. In my experience, they are people of high integrity. They will do what is right. If they think they should comment, they will comment.

Senator SPECTER. Has there been any comment made by anybody on any of the BOC's on any of these subjects to either of you gentlemen?

Mr. TANENBAUM. I have talked to many of them.

Senator SPECTER. Has anybody from one of the BOC's raised any objection to you, Mr. Tanenbaum, about the settlement?

Mr. TANENBAUM. I do not think any of them are happy with it any more than we are, sir. We are not happy with the whole situation. As I said, we liked the way the telephone company was run many years ago in that environment. At the same time, I think they all realize, understand, and generally agree with the fact that this was the decision we had to make at this time, and they are supportive of it.

Senator SPECTER. So none of the employees of the BOC's feel that the BOC's have been unfairly treated or are getting the short end of the arrangement in contrast with the AT&T position which will emerge after the divestiture?

Mr. TANENBAUM. I cannot speak about all the employees of the telephone companies. I have not talked with all of them.

Senator SPECTER. I am talking about anyone who has commented to you.

Mr. TANENBAUM. As to everyone I have talked to about this, they do not like the restrictions that are placed on them. They do not like the idea of divestiture any more than we do. At the same time, they do not like the other things that were also going on and the restrictions that were going to be put on the company as a whole.

I think everyone I have talked to generally agrees with the fact, considering the present situation and looking into the future at how the business was going to emerge, that this was the best solution for all parties.

Senator SPECTER. Senator Thurmond's ninth question: The proposed modification contains no provision regarding the licensing of patents by AT&T as had been provided for in the 1956 consent decree. In light of this, what is AT&T's intention with respect to the licensing of its patents?

Mr. TANENBAUM. I think our intention is to look at that situation like any other competitive company would look at the similar situation and to license patents where we think it is in the best interests of the company to do that, just like IBM, RCA, IT&T and every

other company with whom we will be in head-to-head competition does.

Senator SPECTER. Do you have anything to add to that, Mr. Trienens?

Mr. TRIENENS. No. I think there will be a lot of cross-licensing as there is today and as there is among American industry generally.

Senator SPECTER. Senator Thurmond's 10th question: The proposed modification uses the terms Bell operating companies and AT&T. Will the BOC's continue to use the Bell name and logo?

Mr. TANENBAUM. That is something that really just has not been worked out yet. I do not know what the legal ramifications of that are or just what will happen there.

Senator SPECTER. Do you have anything to add to that, Mr. Trienens?

Mr. TRIENENS. No. That is under very active study right now.

Senator SPECTER. Senator Thurmond's 11th question: In your view, is legislation still necessary to deal with the problems we have been discussing today? If so, do you think that S. 898 is an appropriate framework for that legislation?

Mr. TANENBAUM. There are of course a number of issues that this decree does not treat and cannot treat. The general conceptual framework of S. 898 as I read it is a determination on the part of the Senate that in the future competition should be the rule in telecommunications, that regulation should be restricted and applied only where absolutely necessary.

If that is the sense and determination of Congress, then I think some legislation is required to so state that because clearly the 1934 act, which as we all know was written in an altogether different era and a different time, does not convey that intent.

However, I think the most important thing, as Professor Baxter has indicated, is that this decree substantially and in major ways changes the whole structure of the industry, ways in which even we who have known about it a couple of weeks longer than the rest of the world do not and cannot fully understand.

It is most important for everyone concerned with legislation, particularly with the hope that I am sure you would share that legislation really ought to try to set the course of the industry for the next 20 years or so because we need that kind of stability, as any business does, in terms of the boundary conditions under which it is going to operate, that that kind of legislation really needs to be thoroughly reconsidered and thoroughly understood with this new proposed structure. We would hope that would be done and the Congress would then determine in its own wisdom what should be done with regard to legislation.

Senator SPECTER. Mr. Trienens, do you have anything to add to that?

Mr. TRIENENS. No, sir.

Senator SPECTER. Senator Thurmond's 12th question: What effect do you think the proposed modifications will have on foreign competition in the telecommunications industry in this country and on AT&T's ability to compete abroad?

Mr. TANENBAUM. One of our desires, and I think one of the desires of the Department of Justice both in the structure of this decree and particularly in removing the restrictions of the 1956

decree, was to provide just exactly the kind of flexibility and the ability to keep together the resources of Bell Laboratories and Western Electric unhampered and unimpaired so that they can compete fully.

I do believe that this decree is perfectly consistent with our continuing ability and in fact an enhanced ability because of the removal of the restraints of the 1956 consent decree.

Senator SPECTER. Do you have anything to add to that, Mr. Trienens?

Mr. TRIENENS. I think that is a critically important point. The whole economic thrust of this disposition of our controversy with Justice is to enable the company to better compete not only in telecommunications but the other areas where the distinctions have blurred—computers and data processing—and wherever the technology takes you, to compete not only in this country but to keep our leadership in world trade in these areas.

As we have said before, this is not our preferred choice. Those of us who grew up in this business would like to have the restricted entry, the monopoly, the entire integration both horizontally and vertically. However, for the reasons suggested in the question this choice is far better than some of the other choices that were in front of us, one of which would be the threat—why not just divest Western.

Divesting Western and maiming Bell Labs was the worse thing to do in terms of our technology and in terms of foreign competition. Some of the things do not seem so bad when they appear in the form of legislation, but almost as bad are the kind of restrictions we were threatened with and indeed that in many cases were imposed on us in various legislation proposals which would have, if not divested Bell Labs, so crippled its internal operations and its information flows and other things that it would have disabled it from effectively getting its technology out and competing in foreign trade.

While it is not the "good old days" preferential choice, this choice is far better for the reasons indicated in that question than were some of the other alternatives that were available.

Senator SPECTER. Senator Thurmond's 13th question: Do you have any concerns about one or more of the BOC's being acquired by a competitor either foreign or domestic?

Mr. TRIENENS. In terms of being acquired by a competitor, if that competitor—I do not know who he has in mind—has anything to do with interexchange operations, customer premises equipment, or any of these other items which the BOC's are forbidden from entering because of this so-called leveraging of their natural monopoly in other fields, anybody who has those lines of business could not acquire a BOC. That very much limits who might buy them.

Exxon could not. Maybe Marathon could have. It does not seem likely, but the kind of company you would expect might want to buy a BOC in order to help their customer premise equipment business or some other business are simply barred by the decree from doing it.

Senator SPECTER. You say Exxon could not buy it?

Mr. TRIENENS. That is because they are in the customer premises equipment business.

Senator SPECTER. How about Mobil?

Mr. TRIENENS. I would not want to comment on what Mobil might want to do.

Senator SPECTER. Mr. Tanenbaum, do you have anything to add to that answer.

Mr. TANENBAUM. No.

Senator SPECTER. Would you care to comment about Mobil?

Mr. TANENBAUM. I suspect that Montgomery Wards probably sells some telephones in its stores, but, no, I would not comment about Mobil.

Senator SPECTER. Let us take a very short recess at this point.

[Recess taken.]

Senator SPECTER. I regret the short delay. I had not anticipated presiding at these hearings all afternoon. Probably you had not anticipated being here either.

There are still a few more questions which are on the agenda from Senator Thurmond's list. The next one is: What local exchange telecommunication services may a Bell operating company engage in? For example, may it engage in cable TV distribution?

Mr. TRIENENS. As far as the decree is concerned, if it is transmission of signals within an exchange area or intraexchange services, the decree does not prohibit it. There are a lot of regulations over at the FCC and otherwise that deal with who can be in and who cannot be in CA TV, but the decree does not affect that.

Senator SPECTER. Cellular mobile radio?

Mr. TRIENENS. That would be an exchange service. The decree does not prohibit or tell the BOC's what kind of technology they can or cannot use in providing exchange services.

Mr. TANENBAUM. We think that is very important that they be able to use any technology that is available to them.

Senator SPECTER. Therefore they could engage in cellular mobile radio insofar as the decree is concerned?

Mr. TANENBAUM. Yes, sir.

Senator SPECTER. Digital termination system?

Mr. TRIENENS. It does not distinguish between digital or analog or whatever the technology.

Senator SPECTER. That would be acceptable for the Bell operating company to engage in the digital termination system then?

Mr. TANENBAUM. As I understand that system, it is used for the local distribution of digital signals, the intraexchange of digital signals. I think that would come under the category of intraexchange service or intraexchange access service and they could be in it.

Senator SPECTER. They could be in it.

Mr. TANENBAUM. That is my understanding.

Senator SPECTER. Multipoint distribution system?

Mr. TANENBAUM. Again, anything that is a local exchange service and to the degree that those multiple points are all within a single exchange, they could be in it.

Senator SPECTER. Do you have anything to add to that?

Mr. TRIENENS. I do not.

Senator SPECTER. Does the multifunction facility sharing provision of the decree apply to facilities constructed after the date of the decree?

Mr. TRIENENS. It does not prohibit arm's-length transactions of that sort with anybody. The answer is, yes, it would extend beyond the decree.

Senator SPECTER. You are nodding agreement with that, Mr. Tanenbaum?

Mr. TANENBAUM. I am in agreement with that; yes. The operating companies are permitted to enter into those kinds of arrangements as described in the decree before, during, or after and with anyone.

Senator SPECTER. Mr. Baxter stated that there are no statutory entry barriers to long-distance service. Do not some, if not most, States require intrastate toll carriers to obtain certificates of public convenience and necessity prior to providing service?

Mr. TRIENENS. As I understood Mr. Baxter, he was referring primarily to the long distance or interstate. What you say is true as to intrastate, at least so long as the present jurisdiction holds. I put that caveat on it because of pending legislation that would change it.

Senator SPECTER. Is there anything in the decree to indicate that the patent licensing provisions of the 1956 decree will continue to apply to existing patents?

Mr. TRIENENS. No; but we do have patent licensing agreements out that are valid and binding usually for the life of the patents.

Mr. TANENBAUM. That is my understanding. Those agreements are still valid.

Senator SPECTER. A subpart of this question is, For how long will these licensing provisions apply?

Mr. TRIENENS. The life of the patent.

Senator SPECTER. Let us go back to the business about subsidies and start again. In my view, this is the central question in the public interest arena. Perhaps we could start, Mr. Tanenbaum, with your explanation as to what subsidies are currently given to local Bell operating companies.

Mr. TANENBAUM. If I might take just a moment, Senator, I might be able to do a little better job than I think I did in an earlier response to you in trying to explain how the present system works in terms of the subsidies that flow from long distance to local exchange.

The problem arises because the local facilities—that includes the telephone, the wire from your telephone to the central office, and a part of that central office—are used for both local service and for long distance service. When you pick up your telephone, until you dial the number, nobody knows whether you are going to make a local call or a long distance call. You have to use the same telephone and the same wire.

That is what we call the nontraffic-sensitive plant. The reason we call it that is you have to have a telephone no matter how much you use it and you have to have a wire to the central office no matter how much you use it. As to that kind of plant which is jointly used for both services, you have to decide how you allocate the costs of that.

If you go back prior to about 1930, the rates for that wire, that local plant, were covered entirely by local rates. I think that is the time period.

Mr. TRIENENS. Prior to *Smith* v. *Illinois Bell.*

Mr. TANENBAUM. There was a classic case that went to the Supreme Court, *Smith* v. *Illinois Bell,* where the Supreme Court decided that that was not quite fair, that because that local plant was also used for long distance calling some of the cost of that ought to be allocated to long distance and be paid for by the people who use it for long-distance calling.

As it started out, the immediate question was how do you make that allocation? It is there whether you use it or not. It would cost you the same amount no matter how much you use it for either of those same services, to put it in, to maintain it, and what have you.

A system first appeared where a decision was made that probably the best way to allocate it is based upon how much it is used. If it is used so many minutes a month for long distance, 10 minutes a month for long distance, and 90 minutes a month for local calls, then 10 percent of the costs ought to be allocated to long distance and 90 percent ought to be allocated to local.

Over a period of time, however, technology intervened. What technology did was it started driving down the costs of carrying long distance calls much more rapidly than it was able to drive down the costs of local service. With the microwave radio systems and all kinds of electronics, those costs started coming down very rapidly.

The regulators were then faced with the question of do we reduce the rates of long distance calls while the rates of local calls are going up because inflation is having its effect there. The conclusion was made that it was very important to keep the cost of local service low. Instead of lowering long distance rates and letting the costs of local service go up, they said, "Let us change the allocation." They said, "Really, when you are using those local facilities for long distance calls, they are more valuable than when you are using them for local calls because you are calling a longer distance and that whole service is more valuable."

Through a series of agreements, various separation agreements usually named for the place where those agreements were finally concluded—these were agreements between the State regulators and the Federal regulators—they arrived at a series of methods of how those costs would be allocated.

The latest agreement was called the Ozark agreement because it occurred at a meeting in the Ozark mountains. That agreement has resulted in the fact that today, although the average usage for long distance calls of the average local plant usage is about 8 percent, the amount of costs that is allocated is about 26 percent. That is 8 percent for long distance on the average.

We do studies of this continuously. Although it is used only about 8 percent for long distance, about 26 percent of the cost is allocated to the long-distance service as a result of this Ozark agreement.

When you allocate those costs, now the rates are determined in the two jurisdictions. The costs in the interstate jurisdiction are higher because you have allocated more costs there and so the rates are higher. The costs in the local jurisdictions are lower because you have allocated some of the costs away and so those local

rates are lower. That is what we mean when we talk about the cross-subsidy.

You can argue, "Is that a cross-subsidy or is that not a cross-subsidy?" It all depends on how those costs are allocated. However, if you accept the principle that probably the most rational way to allocate those costs depends on how the facilities are used, then you would say there is a substantial cross-subsidy that flows from the long distance to the local by moving the costs out of the local.

I do not know whether that is any clearer or not, but that is what really happens.

Senator SPECTER. Why did AT&T in its overall planning choose to allocate the costs in the way to keep the prices of local calling down while the costs of long-distance prices were kept up?

Mr. TANENBAUM. Senator, we do not have the choice of how that is done. That is done by the regulators. The regulators make that decision.

Senator SPECTER. Do they make the allocation of costs as between local and long distance?

Mr. TANENBAUM. They tell us in detail through a manual called the separations manual. They tell us in detail how those costs are to be allocated.

Mr. TRIENENS. Although originally the product of negotiations between the State regulators and the Federal regulators, since 1967 that manual has been an FCC rule published in the Code of Federal Regulations and binding on us just like a statute. The only way that can be changed—and the way that this joint board that I spoke of earlier recommends it be changed—is by an amendment to the Code of Federal Regulations which changes the rule telling telephone companies how to allocate the costs.

Mr. TANENBAUM. In all candor, I ought to add that we did not strongly resist these changes. We argued about them from time to time, but we believed also that it was important to keep the cost of local service down to make service universally available. That is how we read the mandate of the law in the 1934 Communications Act.

Senator SPECTER. You say AT&T did not strongly resist the allocation.

Mr. TANENBAUM. We acquiesced. We never went to court on it. Let me put it that way.

Senator SPECTER. May we expect AT&T to continue that attitude of either not strongly resisting or acquiescing?

Mr. TANENBAUM. Senator, as I have said, we have been saying for the last 10 years that that system has got to change. You can have that sort of thing, you can have this kind of arbitrary allocation of cost when you have a single supplier monopoly environment. As soon as you have a competitive environment people will come in to that high priced service that is carrying the subsidy and undercut that price because that price is above what it actually costs you to provide it.

Senator SPECTER. Mr. Tanenbaum, the essential question is, Will AT&T's attitude be different after divestiture on this subject than it has been before divestiture?

Mr. TANENBAUM. No, sir, absolutely not.

Senator SPECTER. Will you still love the local consumer the same the morning after?

Mr. TANENBAUM. Since he provides our bread and butter, the answer to that is, "Yes."

Senator SPECTER. Excuse me?

Mr. TANENBAUM. I said since the consumer provides the bread and butter—it is the prices they pay that give us the revenues that keep the business——

Senator SPECTER. However, AT&T will not care about the local consumer after divestiture.

Mr. TANENBAUM. We will care about the local consumer in many ways. We will be selling him customer premises equipment. We will care about the fact that if the prices for those local facilities are too high he is not going to do as much long-distance telephone calling. We have a great interest in terms of making it possible for everybody to have a telephone so they can buy telephones from us and so they can make long-distance calls.

Senator SPECTER. You still have another interest. You still have an interest, but you have another primary relationship, which is the concern. Your primary relationship is now on other lines. It is an irrelevancy in your overall profit picture whether you allocate to your vest pocket or your rear pocket.

Mr. TANENBAUM. It is no longer an allocation, Senator. It is now a payment that we have to make to a completely independent company.

Senator SPECTER. You would be more likely to resist the payment than to resist the allocation among your pockets.

Mr. TANENBAUM. The principal thing we would be concerned about is what we are concerned about today, that one of the services that we are offering is open to competition and is priced too high because it is paying subsidies to another service, the local service, which is not open to competition.

That means that people can come in and compete with us unfairly because they do not have to pay those high subsidies. That has been of concern to us up to this point. It will continue to be of concern.

Senator SPECTER. How many competitors do you have on the long-distance lines at the present time?

Mr. TANENBAUM. Today there are over 200 other common carriers, domestic satellite carriers, resale carriers that serve over 300 communities in 43 States. Their services are available to 60 percent of the total U.S. population and about 90 percent of the people in urban areas can buy long distance services from competitors.

Senator SPECTER. Nonetheless, all that totals up to is about 3 percent, right?

Mr. TANENBAUM. Today, after only 3 years since they have really been in this business, they have about 4 percent of the market. The OCC's are doubling their share every year. They say that they expect that to continue for several years. If they succeed in doing that, in another 3 years they will have about one third of the market.

This is changing very, very rapidly, Senator, and it is of great concern to us. It is a very competitive market. Professor Baxter realizes that. That is why he points out very clearly that he believes

the long-distance business is competitive now—rapidly growing very much more competitive—and that is why he suggests that serious thought ought to be given to the deregulation of that business.

Senator SPECTER. Absent divestiture, what do you think AT&T's attitude would be 5 years down the road or 10 years down the road concerning these allocations between local and long distance?

Mr. TANENBAUM. It would be the same that it has been; namely, that with competition in that market you cannot sustain those kinds of subsidies and they must disappear.

Senator SPECTER. However, so far, as you say, you have been acquiescing.

Mr. TANENBAUM. No, sir.

Senator SPECTER. You have not been?

Mr. TANENBAUM. That was 10 years ago. As I pointed out, for the last 10 years we have been making this point. Why 10 years ago? That is when the first decisions were made to let competition in this business. We have been pointing out to the regulators——

Senator SPECTER. However, you have not gone to court over the issue is what you testified to.

Mr. TANENBAUM. I said that with regard to the separations plan, and Ozark is more than 10 years old, we have been arguing in the Congress and the Congress has recognized this by mandating access charges and by mandating access charges that are cost based. They have recognized this.

We have been arguing it before the FCC. As Mr. Trienens has pointed out, the joint board, FCC and State regulators, have taken action to start acting on this. We have been making this point. We will have to continue to make it. We would make it with or without divestiture.

Senator SPECTER. Up to now, how much, if at all, have local telephone rates gone up as a result of your change in attitude?

Mr. TANENBAUM. With regard to the subsidy?

Senator SPECTER. Yes.

Mr. TANENBAUM. The first action recommended to change the subsidy is recommended to go into effect as of the first of 1982, January 1, 1982. With regard to that particular aspect, that is just starting to happen.

A number of other related things have been going on. One of the most important of those is a recognition on the part of regulators that depreciation rates have been held too low and that depreciation rates have to go up because of technology and because of the effect of competition also on the life of equipment.

There has been action over the last few years—the most significant one only a few weeks or a few days ago; the most recent FCC action was Thursday of last week—again recognizing the need to increase depreciation rates. All of those things have upward pressure on local rates.

Senator SPECTER. Would you amplify what you mean by increasing depreciation rates?

Mr. TANENBAUM. There are a number of factors that go on there. Let me talk about one aspect. It has to do with the wiring inside your house or business.

In the past, we put that wiring in and charged only a nominal fee for what it cost to put that wiring in. We expected to recover it in monthly rates over a long period of time.

The FCC has recognized that in a competitive environment with customer premise equipment you cannot do that any longer. They have said that instead of capitalizing that and recovering it over a long period of time you have to expense it when it is done and now go back to the State regulators and get those rates increased so that the person who has the equipment installed pays the cost of that. This is one aspect of where we have gone from very, very long times to doing it quickly.

The FCC has also recognized with new technology, electronic switching machines, that the old electro-mechanical switching machines that we have been using have been written off too slowly. They are becoming technologically obsolete much more rapidly than the depreciation rates would recognize. The depreciation rates may have assumed they would last 30 years. They are not lasting 30 years. New technology is coming in that is more attractive. They are being taken out sooner and replaced sooner. We have to recover that capital.

We had never been permitted to set depreciation rates at levels that we thought were economically justified. They have always been mandated by the FCC in customer premise equipment, PBX's, and things of that sort. The old electro-mechanical PBX's are rapidly becoming obsolete by new electronic ones, much more rapidly than was assumed by the FCC, and those rates have to go up.

There are all these factors which say you have to recover your capital investment more rapidly because the equipment is not going to live as long. What does that do? That tends to increase the cost of the business and put more pressure on local rates and long distance rates.

Senator SPECTER. Mr. Tanenbaum, it is obviously an extraordinarily complicated matter with a lot of dimensions and a lot of facets. However, on the very bottom line, would you not concede that at least to some extent the local telephone consumer would have lower rates if AT&T stayed together than if you had divestiture?

Mr. TANENBAUM. In the current scenario with competition and with all the things that are happening, I would not agree with that. I would not agree with that.

As I said before, if you want to go back to a fully regulated noncompetitive environment, then we really believe that the kind of organization and structure that we did have fit that perfectly. It fit it very well. It enabled us to build the best telecommunications system in the world.

However, the trade-offs one has to pay here to introduce competition among those, we believe, is a change in the structure of the Bell System.

Senator SPECTER. You are saying that the local user will not pay more ultimately with divestiture than absent divestiture in your opinion.

Mr. TANENBAUM. Yes, that is my opinion.

Senator SPECTER. Do you think they will pay less?

Mr. TANENBAUM. That depends upon the confidence you have in competition.

Senator SPECTER. Wait a minute. What competition is there going to be on local telephone service?

Mr. TANENBAUM. I am sorry. There is going to be competition in the customer premise equipment that he is going to use, his telephones and what have you. The Justice Department believes there will be more competition now in the supply of equipment to local telephone companies. We believe there has always been that competition and the companies have made their decisions based on economics.

Senator SPECTER. You do not think there will be lower costs of equipment.

Mr. TANENBAUM. No, I do not believe there will be.

Senator SPECTER. In what way, in your opinion, will there be a lower cost to the local telephone consumer?

Mr. TANENBAUM. Senator, I cannot guarantee you that there will be a lower cost.

Senator SPECTER. I am not asking for a guarantee. I am asking for even a suggestion, a possibility, a glimmer of hope.

Mr. TANENBAUM. I just have to tell you as I told you before that I do not believe that this decree is going to affect that in any significant way, that the forces that would either drive those local rates up or down are there anyway. They are happening anyway. That is what led us to the conclusion that we should accept the conditions of this decree.

Mr. TRIENENS. I will give you a suggestion, Mr. Chairman, as to why this will relieve the pressure on local rates. It is like the old story of "compared to what?"

It should have been apparent with the passage of S. 898 and with other things going around town both on the Hill and at the FCC that this company was not going to be permitted to keep its size and keep its perceived power over these local monopolies in the absence of continued restrictions like the 1956 decree and added restrictions like procurement quotas, market tests—these open market tests applicable to the purchase of exchange equipment—like a dozen of other separations and information flow restrictions that would impede the labs.

Compared to those kinds of restrictions, each of which introduced inefficiencies and made this business more difficult to run, this is a much less burdensome, a much cleaner and more efficient way of accomplishing the problem.

As Mr. Tanenbaum says, if you would just brush away all those restrictions, brush away the 1956 decree and go back to the good old monopoly days, unrestricted, that would be terrific. The integrated system, horizontally and vertically, would be the way to do it, but that is not the world we are in.

Senator SPECTER. After divestiture, what assurances will there be that the local operating companies will have the ability to borrow money with bonds at a premium rating?

Mr. TRIENENS. There are two answers to that, the first of which is that upon divestiture the company has undertaken, and it will be demonstrated, that these companies will go out as viable companies with attractive capital structures appropriate to their business

and will be in a position to finance and continue to provide public service in their local areas.

Thereafter, just as today, the ability of a local company to attract the capital to meet the construction needs of its community will depend on its earnings. That will depend on the rate of return which is not only authorized but in fact allowed by the regulatory commissions. That is not too different than it is today. It will simply focus on the areas in which those companies operate.

Senator SPECTER. Does AT&T have any expectation of getting into the cable TV business?

Mr. TRIENENS. No.

Senator SPECTER. Has that matter been considered by AT&T?

Mr. TRIENENS. Considered in the sense that I am not giving an off-the-cuff answer. I mean the executives have considered that question and do not expect to get into that business. We expected that question to be asked.

Senator SPECTER. Do you have any expectation when that decision would be subject to re-evaluation? Stated differently, how good is that decision? How long is that decision good for?

Mr. TRIENENS. We have a lot on our hands. There is a lot to be done. As to the idea of going into the cable television business, as a subject of priority it has been decided not to. There is no expectation of that. If you asked IBM the same question, they would have to give you the same answer, that they do not contemplate it now, but who knows?

Bear in mind though that the big problem has been that AT&T should not get into things because they possess the "local monopoly bottleneck." The very thing that drove all these restrictive conditions no longer exists.

Mr. TANENBAUM. I think that is the important question because we certainly do feel strongly that we should not be subjected to any restrictions that others are not subjected to, that we are in a competitive business growing more and more competitive all the time. We require the same freedoms to compete as others in these businesses.

Senator SPECTER. You do not have any expectation at the present time, but you just cannot say when that would change?

Mr. TRIENENS. No more than if you asked the chairman of IBM.

Senator SPECTER. I do not have the chairman of IBM here at the moment.

Mr. TRIENENS. I am guessing you would get the same answer.

Senator SPECTER. I asked Mr. Baxter about this requirement that Judge Greene put into effect that within 15 days from January 21 the court was asking for a statement as to any contacts made by anybody from AT&T with anybody from the U.S. Government, except communications made by counsel of record alone with the Attorney General or employees of the Department of Justice.

I would ask you gentlemen at this time what contacts were made by anyone from AT&T with anybody from the Government with those exceptions.

Mr. TRIENENS. I plan to so certify to the court within the time period. I think I know the answer to that now. I am making a survey of everybody who had any inkling of the existence of this decree, this proposed modification, before it was announced to

doublecheck my information, but I know of five such contacts and only five.

Senator SPECTER. What were they?

Mr. TRIENENS. First was a meeting that I and Mr. Charles L. Brown, the chairman, attended with Mr. Baxter.

Senator SPECTER. No. 2?

Mr. TRIENENS. No. 2 was a telephone call that Mr. Brown made to Mr. Baxter to further clarify the definitions of the decree.

Senator SPECTER. No. 3?

Mr. TRIENENS. Third was a visit that at the time the three of us talked Mr. Baxter suggested should be made. It was made by Mr. Brown visiting Secretary of Defense Weinberger.

Senator SPECTER. When did that meeting occur?

Mr. TRIENENS. That was Wednesday, January 6.

Senator SPECTER. You heard Mr. Baxter's testimony this morning?

Mr. TRIENENS. Yes, sir.

Senator SPECTER. Did you not find it surprising that Mr. Baxter would ask Mr. Brown to make a contact with Mr. Baxter's client, the Department of Defense?

Mr. TRIENENS. No; I did not. While I agree with Mr. Baxter's characterization of its being unusual, what was unusual was not that particular episode but the phenomenon that through 1981 and particularly in testimony before another committee of this Senate, the Secretary of Defense had testified that he believed the pending case should be dismissed.

Senator SPECTER. Excuse me. What?

Mr. TRIENENS. Secretary Weinberger had testified before the Armed Services Committee that the Government's case against AT&T should be dismissed. That I regard as unusual. I think this flowed from that.

Senator SPECTER. Mr. Trienens, have you ever seen a case where a lawyer asked his opponent to communicate with his client on a settlement proposal?

Mr. TRIENENS. I have never seen a case of this character in that and other respects that are parallel, namely the question of who is the client. I never heard of a client going around saying a case ought to be dismissed and the lawyer continuing it either. This is a very unusual situation.

Senator SPECTER. The answer to my question is you have not ever seen a situation like that?

Mr. TRIENENS. I have never heard of either of them. No, I have not heard of such a situation.

Senator SPECTER. The fourth meeting?

Mr. TRIENENS. The fourth meeting was Mr. Brown advised Secretary Baldrige of the intention to settle this case and modify the 1956 decree.

Senator SPECTER. When was that?

Mr. TRIENENS. That was the morning of January 7.

Senator SPECTER. Were you present at that meeting?

Mr. TRIENENS. I was not. As I say, I have the function of certifying to the court these meetings. In that connection, I have conducted this investigation.

Senator SPECTER. However, you have been told what occurred at that meeting?

Mr. TRIENENS. Yes, sir.

Senator SPECTER. What were you told?

Mr. TRIENENS. I was told that Mr. Baldrige, who had been active in formulating telecommunications policy as Chairman of the Cabinet Council on Commerce and Trade, was advised by Mr. Brown of Mr. Brown's intention to enter into the modification of the 1956 decree and therefore dispose of his controversies with Mr. Baxter.

Senator SPECTER. Mr. Baldrige found that acceptable?

Mr. TRIENENS. He did not interpose any objection to my knowledge.

Senator SPECTER. The fifth contact?

Mr. TRIENENS. The fifth contact was to give the same advice to the White House. It is my understanding that present at that meeting were Mr. Meese and Mr. Fielding.

Senator SPECTER. Again, any objection raised by either Mr. Fielding or Mr. Meese?

Mr. TRIENENS. No, sir.

Senator SPECTER. That constitutes the totality of all the contacts between anyone from AT&T to your knowledge with anyone from the Government?

Mr. TRIENENS. Within the meaning of the paragraph you described, yes, sir.

Senator SPECTER. Is there some limitation when you say within the meaning of the paragraph?

Mr. TRIENENS. Oh, yes. There were a number of contacts between counsel of record alone with counsel of record.

Senator SPECTER. Except for that?

Mr. TRIENENS. Except for that, that is correct.

Senator SPECTER. I am advised that a January 8, 1982, news bulletin of Bell of Pennsylvania and Diamond State Telephone stated:

> AT&T said it would take whatever steps are necessary to maintain the financial viability of the Bell System's operating companies during the transition period.

Do you know if that is an accurate statement?

Mr. TRIENENS. Yes. That is totally consistent with what Mr. Brown has said publicly.

Senator SPECTER. What steps are contemplated during such a transition period?

Mr. TRIENENS. What steps are contemplated during the transition period?

Senator SPECTER. Yes.

Mr. TRIENENS. One of them is to enable them to finance their construction programs and to help them, as we have in the past, to do that.

Senator SPECTER. How do you accomplish that?

Mr. TRIENENS. We help them both by positioning and scheduling their bond issues, by helping them with short-term financing, and by infusing new equity.

Mr. TANENBAUM. If I might just add, we will help them most, I think, by getting the uncertainty surrounding all of this completed and getting the job done.

Senator SPECTER. I am advised that Mr. Brown has been quoted as saying that the local companies will be divested:

> In sound financial condition, well positioned in a growth industry, and possessed of all the necessary resources to prosper as they acquire new technologies and continue to enlarge the usefulness of communication service.

My question is if you know that to be an accurate statement.

Mr. TRIENENS. It sounds accurate, yes.

Senator SPECTER. Where does the settlement leave S. 898?

Mr. TANENBAUM. Senator, I guess I can only answer that by the discussion we had before. S. 898 of course envisioned an altogether different industry structure. A large part of S. 898—I think Professor Baxter said maybe 90 percent of it; I do not know what the quantification is but certainly a large part of it—was directly tailored to the kind of industry structure that existed and everyone expected to exist prior to this modified consent decree.

It seems to me that S. 898 really must be revisited in substantial part in light of this new structure. This consent decree was intentionally written in a way to be as consistent as we could be with what we believe the basic principles underlying S. 898 were and what the Congress, as far as we could interpret it, was trying to accomplish, namely, a much more competitive environment, the assurance of equal access for all providers of long distance service to the local bottleneck, and the removal of any possibility of unfair cross-subsidies from regulated to nonregulated business.

However, the decree of course does not have the same statutory authority that the Congress has, so there are many other areas that the decree could not deal with. We expect that the Congress may very well want to deal with those.

However, we think it is most important that there be a good and complete understanding of what this future structure is likely to be, what it is going to look like, and how it is going to work before new law is written that hopefully will have effect and force for a long period of time.

Senator SPECTER. It would be your position then that the House ought not to act on S. 898 in its current form.

Mr. TANENBAUM. I think that certainly would not be appropriate. There are things in S. 898 that just do not apply anymore.

Senator SPECTER. Does AT&T have any plans to engage competitively with the newspapers like the Washington Post or the New York Times. As I understand, it would be free to do so with the change in the 1956 decree?

Mr. TANENBAUM. We do not plan to go into the newspaper publishing business, Senator. We never have.

Senator SPECTER. You could if you wanted to though under the modification of the 1956 decree.

Mr. TANENBAUM. We could as any other business could.

Senator SPECTER. However, you have no plans to do so?

Mr. TANENBAUM. We certainly have no plans to do so. I cannot envision the time myself when we would think we could be successful in the newspaper publishing business. That is an altogether different business and requires talents and resources that we just do not have.

Senator SPECTER. It requires talents that you do not have?

Mr. TANENBAUM. We do not hire any reporters.

Mr. TRIENENS. I should note that the concern that was so eloquently expressed by the publishers and which led to the amendment that was included in S. 898 was directly tied to the possession of the local exchange bottleneck and that he who controlled that bottleneck should not have anything to do with the content that went over that bottleneck. That problem is gone. The local exchange company cannot put content over that line and AT&T will not own that line. That whole problem is gone.

Senator SPECTER. Do you have any expectation of entering into the electronic information services?

Mr. TRIENENS. In terms of the same concept, in terms of owning the access to the home and putting content over that access, that cannot happen under this divestiture. In terms of AT&T's interest in working on the terminal equipment, the data bases, and other material that might be used in connection with and under tariff rates with in an unaffiliated local distribution system, yes, there is a continuing interest.

Mr. TANENBAUM. We think we have a lot of talent to bring to that particular market. There are a lot of large companies that are very interested in that market. Our plans are in no way firm, but we certainly think that that is something we ought to be considering and decide whether it is a good business or not.

Senator SPECTER. With the genius of Bell Laboratories now free, should this settlement be approved and pass muster at all steps along the way, would it be your expectation that Bell Laboratories would now have great potential for very imaginative new ideas and new ventures?

Mr. TANENBAUM. That is certainly our hope and expectation and one of the strong points particularly with regard to international markets both in terms of competing with foreign suppliers as they come here and our ability to compete in foreign markets.

Senator SPECTER. Can you give us just a thumbnail of what you might be looking toward in that respect, something specific, without giving away any big secrets?

Mr. TANENBAUM. I could talk at great length about the kinds of services that we are proposing to offer now. My attorney here would get a little angry with me if I talked too much about things that are on the horizon before they are developed and we are ready to present them.

Senator SPECTER. Do not anticipate your attorney's objections. Start off and see what he says.

Mr. TANENBAUM. One thing I would point to immediately is a service where we have asked the FCC to permit us to establish a separate subsidiary, as we must today under their requirements, for something called Advance Communication Services. That is a data service of interest to both large and small businesses which will permit computers of different manufacturers and computer terminals of different manufacturers to communicate with each other in ways that they cannot do today because they tend to speak different kinds of data languages.

It will provide other enhanced services where customers can store their own computer programs and access them from the heart of the network. We think it will be a valuable service and a

service that on a network basis can be made available to a lot of small businesses that might not be able to build their own systems the way very large companies do.

Senator SPECTER. How close are we to the device where when the phone rings and you can find out who is calling before you pick up the phone?

Mr. TANENBAUM. That is a service that I would expect to see us be able to provide within the next couple of years. It is based on a system we call CCIS, which is a data network that permits the number of the phone that is calling to be transmitted very, very rapidly to the far end. That is the kind of service that requires close cooperation with the local exchange companies.

Senator SPECTER. If someone calls from a pay phone, you will not be able to tell.

Mr. TANENBAUM. You will be able to know the phone number. That is all you will ever know. You will not know who is calling. All you will know is the phone number of the phone that is calling.

Senator SPECTER. Will there be some video arrangement down the line where you can see the person's face regardless of where he is calling from?

Mr. TANENBAUM. That is possible. We could provide that now if you wanted it, but it would be very, very expensive today and you could not do it over normal telephone lines. This other service could be provided over normal telephone lines. It depends on our electronic switching systems. It requires the proper programs to be put in both in the long distance network as well as the local network. That whole program is moving forward.

Senator SPECTER. Mr. Tanenbaum and Mr. Trienens, we very much appreciate your coming in. I am sorry to keep you so late this afternoon. We will be submitting some questions to you in writing. We would like to have those answered within the customary 2-week period after submission. Again, we appreciate your being here this afternoon. Thank you.

The hearing stands adjourned.

[Whereupon, at 4:35 p.m., the committee recessed, to reconvene at the call of the Chair.]

[Material follows:]

Statement of

MORRIS TANENBAUM

My name is Morris Tanenbaum. I am Executive Vice President of the American Telephone and Telegraph Company. I am joined today by Howard J. Trienens, our Vice President and General Counsel. We welcome the opportunity to appear before this Committee to discuss the agreement reached between the U.S. Department of Justice and AT&T which modifies the 1956 Consent Decree.

I will address the 1982 Decree, including a brief description of the Decree and the reasons for its negotiation. I then will discuss the impact of this action, after which Mr. Trienens will discuss the procedure used in filing the Decree and its current status.

THE 1982 CONSENT DECREE

Description of the Decree -- For reasons I will discuss in a moment, the 1982 Consent Decree is a modification of the 1956 Decree. Under the terms of the modified decree, AT&T would divest the local exchange operations of 22 Bell Operating Companies (BOCs) -- the facilities by which customers complete local calls and gain access to long distance and international networks. Such facilities represent approximately two-thirds of the Bell System's total plant, or over $80 billion in assets. The divested Local Exchange Companies (LECs) are required to provide equal access to their local services to all interexchange carriers and information service providers under terms virtually identical to those contained in S. 898.

All Bell System interstate long distance facilities and

portion of the intrastate long distance facilities now owned by the BOCs, will remain part of AT&T after divestiture. Ownership of customer premises equipment also will be retained by AT&T, along with the Western Electric manufacturing subsidiary and Bell Laboratories.

Of the Bell System's approximately one million employees, about half will work for the new LECs upon divestiture while the other half will work for AT&T and the units affiliated with it.

According to the modified decree, the divestiture will take place within 18 months of its acceptance. A plan for reorganizing the Bell System to accommodate this divestiture must be filed with the Department of Justice within six months of the effective date of the modified decree.

Effect of Removing the 1956 Decree -- Termination of the 1956 Consent Decree -- our cornerstone of the agreement to divest the local exchange operations -- removes restrictions and imposed by that Decree on AT&T. This action, along with preserving Bell Laboratories and Western Electric as integral parts of AT&T -- technologically integrated with the Bell System part of the nationwide network -- promises to be a key element in maintaining America's world leadership in the Information Age and in the technology on which that leadership is based. The benefits derived through replacing the 1956 Decree with the new decree will enhance the competitive viability of the Bell System in overseas markets which has obvious benefits with respect to the U.S. balance of trade.

Reasons For Negotiating A Decree -- Over the last several years there has been major change in the technology of communications including a continued blurring of the distinctions between communications and data processing technologies. The nationwide public switched network is in fact the world's largest special purpose computer with that special purpose being communications.

Clear signals have been emerging from the deliberations of Congress, actions of the FCC, and actions of the courts that with the evolution of telecommunications and its use the public interest is best served by a competitive marketplace -- a marketplace in which technology and entrepreneurial ingenuity can be exercised to their fullest to bring products and services of the Information Age to all Americans with regulation limited to basic telecommunications service where effective competition is not yet possible.

The modified decree preserves and indeed further stimulates the flow of technology from Bell Laboratories. It enables us to provide to the public Information Age products and services far sooner than if we had elected to continue to seek resolution of the uncertainty surrounding the future role of the Bell System in other forums and continued to bear the restraints of the 1956 Decree. The modified decree should simplify the deliberations of the Congress as it seeks to update the outdated Communications Act of 1934 -- the issue of Bell System size and structure is no longer a stumbling block.

IMPACT OF THE MODIFIED DECREE

Impact on Rates -- At the beginning let me emphasize that

the upward pressure on local telephone rates that we have been talking about for years and that has been so prominently featured in discussions recently is not a result of the modified decree. It is the result of today's competitive environment and of inflation. The Bell System has a long, successful history of holding down the cost of its services to the nation's telecommunications users. In a 1927 speech to the NARUC, then President of AT&T, Walter Gifford, spoke about the Bell System's obligation "to furnish the best possible telephone service at the lowest cost consistent with financial safety". The foremost principle underlying the Communications Act is that basic telecommunications services should be available to all people of the United States at reasonable rates.

Over the last decade, records of many hearings relating to the growth of competition in the telecommunications industry have pointed to one inevitable outcome -- rates for all services will be driven toward costs. This, when combined with inflation as a fact of life, inevitably means upward pressure on local rates.

In his appearance before the Subcommittee on Communications of the Committee on Commerce on March 21, 1977, AT&T former Chairman, John D. deButts, said that competition "forces prices inexorably toward cost..." and concluded that "in every State jurisdiction we will have to file for further increased rates for basic exchange service."

In November 1979, the National Telecommunications and Information Agency (NTIA) under the direction of Henry Geller addressed the movement of rates to costs in a competitive environment with particular emphasis on the need to reevalu-

ate the cost allocations referred to within the industry as "separations and settlements". In its "Primer" NTIA stated:

> As competition has been introduced into the provision of interexchange services, there is increasing pressure to reevaluate these allocations. This is so because it will be necessary to price traditional long distance service more closely to the cost of providing that service in order to compete with other carriers offering alternative services.

In his statement before the Commerce Committee on June 16, 1981, Charles L. Brown, our Chairman, pointed out that:

> Down through the years, the telephone companies have priced their services to support the goal of universal service. No longer is this policy tenable. More and more we must relate rates to cost - service by service, customer by customer. That means, among other things, that as they are relieved of the burden of contributing to the support of local service, long distance rates will come down - relatively. Deprived of that contribution - and moreover faced with the need to recover the higher depreciation costs that competition dictates - local rates will go up. No aspect of the transition we face is more crucial than sound management of this basic change.

I wish to underscore that the upward pressure on local rates is not a consequence of the divestiture agreement but of growing competition which ultimately drives rates for products and services closer to their costs. These rates reflect the realities of today's competitive marketplace including inflation and more rapid depreciation of plant and equipment which must continue to employ the latest technological advances to meet user expectations.

Impact On Service -- The Bell System remains committed to the best possible service at the lowest possible cost. The

companies which will be divested in a financially strong position so they can meet this commitment in the future.

Accordingly, the decree requires AT&T to assure that upon divestiture the LECs have sufficient personnel, facilities and rights to technical information to permit them to perform their functions. In addition, for a five-year transition period, AT&T, Western Electric and Bell Laboratories will provide on a priority basis the manufacturing, research and development services needed by the LECs to fulfill their requirements under the Decree.

With established customer acceptance, a strong balance sheet, strong revenue streams from measured local service and access charges, full freedom to apply technology, and the continued oversight of state regulatory bodies, the commitment to the best possible service at the lowest possible cost should continue undiminished in these new companies.

Impact on National Security, Defense and Emergency Preparedness -- The modified decree preserves the unified management of the nationwide public long distance network and, by mandating a central point of coordination in the LECs takes explicit account of national defense and emergency preparedness requirements as required by the Communications Act of 1934. As details of the divestiture are developed in greater detail, these national concerns will continue to be addressed. We will, of course, cooperate fully with the Department of Defense and all other agencies of the Federal Government which have responsibilities in these areas.

Impact on Employees -- The modified decree does not change benefits, including pensions, for active or retired Bell

System employees. Nor will the decree alter any existing bargaining agreements covering Bell employees. Employees will benefit from the resolution of much of the uncertainty which has affected their jobs over the last few years. They will also benefit over the long run as they are employed by financially sound, viable entities in their respective markets.

Impact on Share Owners -- After the divestiture of the LECs, share owners will retain the full value of the assets that currently compromise their investment. The only difference is that their investment will be divided between stock in AT&T and proportionate values in the LECs that will, in the future, operate separately from AT&T. Share owners will also benefit from the operation of financially and operationally viable entities in an environment with reduced uncertainty.

* * *

The modified decree, I believe, is in the public interest. It removes the anticompetitive restrictions applied to the Bell System that were the result of an era of pervasive public utility regulation in a monopoly marketplace. Moreover, it tracks closely the goals contained in S. 898 as approved by the Senate last October.

RESPONSES BY MORRIS TENENBAUM TO QUESTIONS SUBMITTED

BY CHAIRMAN THURMOND

1. The Justice Department has now filed its competitive impact statement (CIS). That document explains the Government's understanding of the proposed settlement in greater detail than the modified decree itself does. Do you agree that the CIS accurately describes the effect of the decree? Please identify specifically any aspects of the CIS that do not accurately characterize AT&T's interpretation of the proposed settlement.

ANSWER The Justice Department's competitive impact statement does not contain any constructions of the modified decree with which we disagree. The accuracy of statements in the CIS as to the effect of the decree after divestiture will, as the CIS states, depend upon the application and enforcement of the Communications Act and State regulatory statutes to the divested entities.

2. What percentage of the nation's intercity transmission service revenues does AT&T receive? Please identify specifically AT&T's market share for the following services and facilities. Wherever possible, identify AT&T's market share for both interstate and intrastate interexchange offerings:

--private line services,
--message toll services,
--digital private line services,
--foreign exchange services.

ANSWER To quantify AT&T's or any other's share of the nation's intercity transmissions service revenues would require quantification of the total revenue in that market. This is not possible because (1) all suppliers of intercity transmission services are not required to report their revenues to the FCC, (2) those suppliers who do report their revenues do not all do so in a consistent manner and (3) a significant portion of intercity transmission services are supplied by organizations for their own use, in which instance a revenue is not meaningful.

However, explosive growth in telecommunications competition, especially within the last year or two, demonstrates that the market is rapidly becoming extremely competitive. For example, in the long distance calling market there are more than 200 other common carriers, domestic satellite carriers and resale carriers offering service in some 300 communities in 43 states. Their services are available to 65% of the total U.S. population and over 90% of the population in urban areas where the highest telecommunications traffic is concentrated. One of the major competitors -- MCI - already has over 700,000 customers and in the last quarter of 1981 doubled its revenues compared to the year earlier quarter. MCI has stated that it sees "no reason this growth rate can't

continue." Other competitors have experienced similar growth rates. If Bell competitors in the intercity long distance market continue to increase their revenues annually at a rate of 50%, which is a conservative projection of their recent performance, these companies will capture about 20% of the market in about 5 years. However, other competitors will also enter the market, further accelerating the growth rate of competition.

In any event, revenue share is misleading, not only because revenues are not measurable or reported in a consistent manner, but because such a number would mask the distribution of who actually receives the revenues. Today the Bell System acts as the collection and disbursal agency - via the separations and settlements and division of revenues processes - for the BOCs and the independent telephone companies. If the Modification of Final Judgment had been in effect in 1981, with access charge payments comparable to current separations levels, we estimate that less than 50% of today's interexchange service revenues would remain with the AT&T interexchange entity.

3. How many areas of the country are there where AT&T is the only provider of intercity service?

ANSWER Competitive long distance services are available to 65% of the total U.S. population in some 300 communities in 43 states. About 90% of the people living in urbanized Standard Metropolitan Statistical Areas have access to competitive long distance services. Moreover, competing carriers, through their own facilities augmented by resale of AT&T services, can and do serve all areas of the country.

Private line and Domsat services are more broadly available and readily extended by the construction of ground stations to every part of the U.S. Private microwave systems are larger in their geographic span than the Bell System's microwave network.

3. (continued) Even where companies other than AT&T provide intercity services, don't they sometimes rely heavily on interexchange facilities they have leased from AT&T"

ANSWER Because of FCC policy of open entry, competitors provide their own facilities whenever they desire, and interconnect with others' interexchange facilities where it is more economical for them to do so.

Competitors are growing rapidly, and sometimes choose to lease facilities initially on new routes or on routes for which there is not sufficient traffic to justify additional construction. Based on the most recent information submitted to the FCC by the

three largest specialized common carriers, 47% of the intercity facilities which they lease are leased from someone other than AT&T.

4. With respect to the extent of market power possessed by AT&T Long Lines, I understand that the Telpak [sic] tariff, which provided multiple private lines as a single offering, was withdrawn in 1981, and users were then faced with a 16% private line rate increase and then a 16% general rate increase. Is there any evidence that a significant number of affected subscribers shifted their business away from AT&T? Please provide us with any studies in your possession that quantify the extent of any such shifts.

ANSWER Withdrawal of the Telpak tariff and subsequent private line and general rate increases took place in May and June of 1981. Telpak would have been withdrawn in 1977, but was delayed by a court order obtained by the United States. The private line rate increases were in response to an FCC order prescribing a cost manual. The general rate increase of 16% represented a rate increase of about 4% per year since the FCC's prior determination of AT&T's cost of capital in 1976.

With the complexities involved in the reconfiguration of private line networks customer reaction has been slow to develop. It will probably be two to three years before the full impact is known.

However, there are indications of decreased demand since the rate increases took effect. First, although the economic downturn may be a factor, private line revenue growth has significantly declined. Second, there are clear indications of customer reaction to the rate activity in competitive revenue losses experienced on several high volume business and government accounts. These types of accounts are generally the first to react to rate changes. For example, for a sample of six customers there has been a 17% decrease in revenues for series 2/3000 channels used for Common Control Switching Arrangements (CCSA) and enhanced private switched communications service (EPSCS) networks.

Moreover, with respect to the general concept of "market power", it is clear that AT&T Long Lines does not and cannot "control" entry into the markets it serves or determine unilaterally the prices it charges for services, the latter being a factor of both regulatory action and the prices of competitive offerings.

5. Is it the intent of AT&T to establish a separate subsidiary for its unregulated activities?

ANSWER Yes, in order to comply with the FCC's CI-II order. We have filed a capitalization plan for Advanced Communications Service and other enhanced services. Later this year, we plan to make further filings with the FCC looking to the January 1, 1983 effective date of CI-II as it pertains to other enhanced services and customer premises equipment.

5. (continued) Does AT&T believe, nevertheless, that the Computer Rules should be modified to eliminate the separate subsidiary requirement?

ANSWER We will comply with the requirements of CI-II. Nevertheless, we continue to believe that the stringency of the CI-II separate subsidiary requirements needs to be restudied, particularly in light of 3 factors: (1) the substantial divestiture called for in the Modified Final Judgment, (2) the growing competitive communications marketplace and (3) the public interest in having AT&T as a strong, innovative, productive, competitive force in all aspects of that marketplace.

Short of "eliminating" the subsidiary requirements, we believe the Commission should modify some of the more onerous conditions imposed by its Computer Inquiry decisions, such as the prohibition against providing transmission facilities within the Detariffed/Unregulated AT&T entity and the requirement to treat embedded and new customer premises equipment differently.

6. Would AT&T oppose the inclusion of structural safeguards between its regulated and unregulated activities in future telecommunications legislation?

ANSWER We cannot answer this question without knowing what "structural" provisions are referred to and whose interests are to be "safeguarded." In general terms, the notion of a structurally separated entity as such is not an insurmountable problem if the organizational requirements and any operational or transactional requirements which may apply to such an entity make good managerial, operational and financial sense, and if such requirements are uniformly applied to all participants in the competitive marketplace. The serious problems with structural separation come in: 1) the conditions and restrictions attached to the lines of business the subsidiary can engage in; 2) the kinds of transactions with other Bell entities and non-Bell organizations that are blocked or impeded; and 3) limitations on how the separate entity may be managed, financed, etc.

We understand the concern that the competitive and non-competitive activities not cross-subsidize one another. But, given the competitive nature of all of its activities after divestiture of the exchange operations of the BOCs, the prior concerns over cross-subsidy should no longer exist. Moreover, as we testified before the Committee in January, cost allocation and accounting mechanisms resolve all legitimate concerns of cross-subsidization. We are concerned when the cross-subsidy issue is used to rationalize discriminatory and penal restraints that would have anticompetitive effects on AT&T, Western Electric, Bell Laboratories and the Bell Operating companies.

7. The settlement requires the transfer of intrastate long distance facilities of [sic] AT&T. Presumably, AT&T will thus be designing, constructing, controlling, and administering the network, while the BOCs [will] still be limited to providing local access. Do you believe this could create any competitive problems for independent equipment manufacturers by making it more difficult for them to obtain access to network information than it will be for Western Electric to obtain such information?

ANSWER No. Depending on the size of exchange areas, we expect that approximately half of the intra-state long distance traffic will remain with the BOCs. In addition, today many non-Bell suppliers provide telecommunications products and services used in Bell System network operations (for quantification, see the answer to Question 8 below) and in independent telephone companies which serve some 20% of U.S. telephones. AT&T's carrier operations have every incentive to procure the best products at the best prices, as do the BOCs. Failure to do so would only impair their ability to compete.

We are obligated, under Computer Inquiry II, to make network information available to all suppliers at the same time and on the same terms and conditions.

It should be noted that it is not accurate to characterize the decree as requiring "the transfer of intrastate long distance facilities to AT&T." AT&T shareowners own stocks in companies that own these facilities today and would own stocks in companies that own them after divestiture.

8. With respect to the types of equipment used to provide long distance telephone service, how much competition currently exists, and are there a significant number of products needed by AT&T Long Lines for which Western Electric is the only current supplier?

ANSWER There is significant competition today from domestic and foreign manufacturers for virtually all of the equipment used

to provide long distance telephone service. Moreover, there are many large and technologically advanced corporations which have the capability of offering such equipment.

It is true that Western Electric's No. 4 ESS is the only suitable product available at this time for certain large toll switching applications because it is innovative equipment where only Western Electric has taken the development and manufacturing risk. However, there are several other manufacturers which currently offer smaller size toll switches.

8. (continued) Besides equipment, what products and services do you expect that Western and Bell Labs will provide to AT&T's long distance operations?

ANSWER We expect that Western Electric and Bell Laboratories will continue to provide research and development and engineering and installation services as well as the maintenance, record keeping, operational support systems and services that are necessary efficiently to plan, operate and manage AT&T's long distance operations. Western Electric and Bell Laboratories' products and services will be used where it is judged that they will be the most effective in the competitive marketplace.

9. Is it expected that Western Electric and Bell Labs will remain intimately involved in the coordination and management of the intercity network?

ANSWER Western Electric is involved in intercity network operations as a supplier of technology and equipment. We believe that it is essential that the technological integration of R&D and the manufacturing operations continue for the AT&T portion of the intercity network. That organizational structure and close integration of functions is essential for AT&T to compete successfully. It is also essential in the public interest generally and to national security and emergency preparedness in particular to continue these relationships in the future.

9. (continued) If so, won't this provide funds and network information that give AT&T CPE operations an advantage over independent manufacturers?

ANSWER The important interface requirements for CPE are those related to the local distribution network to which CPE directly interconnects. Because this interface will be completely under the control of the divested BOCs and subject to FCC standards, the AT&T CPE operations will have no advantage over any other supplier of CPE.

10. Eric Nelson, Western Electric's Director or Purchasing, is quoted in the January 17 New York Times as saying that Western Electric hopes to sell its purchasing expertise to the Bell Operating Companies. In your view, would the recent settlement permit Western to become the prime purchasing agent for the BOCs?

ANSWER Under the terms of the proposed Modification of Final Judgment the Standard Supply Contract between Western Electric and the BOCs must be terminated. The services of Western Electric's Purchasing Department would be one of the options for purchase of telecommunications equipment that the local exchange companies will have. Thus, the former relationship will be severed and any new relationship must be negotiated between the then independent BOCs and Western Electric completely at arm's length.

11. Roughly how many patents does AT&T have today? How many of them were obtained in the past decade?

ANSWER As of March 1, 1982 AT&T owned or controlled approximately 9,750 U.S. patents. Approximately 5,000 of these were developed during the past decade.

11. (continued) How many of them pertain to network transmission? To terminal equipment?

ANSWER Although patented inventions generally have applicability to various products, since January 1, 1971, we have classified the claims of our issuing U.S. patents as applicable to various categories of equipment. Such classification, however, does not represent a determination of actual use of those inventions in the identified categories. The number of patents classified as applicable to transmission facilities, including transmission media such as wire and cable, as of March 5, 1982 was approximately 875 and those classified as applicable to terminal equipment was approximately 575.

12. How many American companies hold licenses to AT&T patents?

ANSWER As of April 1, 1982, we had patent license agreements with 417 American licensees. While the great majority of these are companies, the number includes government agencies, individuals and others. Each license agreement with a corporate licensee includes the right of the licensee to extend sub-licenses to its subsidiaries for so long as they remain subsidiaries. Because the licensee is under no obligation to advise us when such sub-licenses are granted, the total number of American licensee companies is not known to us. It is undoubtedly many times greater than 417.

12. (continued) How many foreign companies?

ANSWER As of April 1, 1982, we had patent license agreements with 215 foreign licensees. As explained in the previous answer, because corporate licensees have the right to sub-license their subsidiaries, the actual number is undoubtedly much greater.

12. (continued) How many companies have applied for licenses but have not yet received them?

ANSWER Requests for licenses--new, supplementary and replacing--are received and acted upon continuously. The number of requests being processed at any particular time will vary. Also, often a company requesting licenses will change its mind before the license agreement is executed. As of March 5, 1982, our attorneys were preparing patent license agreements in response to 20 requests.

13. Is it the case that monopoly ratepayers have paid for work that will lead to AT&T patents that will not be issued until after the restructuring occurs?

ANSWER No. Bell System ratepayers have paid for telephone service received, under tariff, from the Bell Operating Companies. The Bell Operating Companies use the revenues received from the ratepayers to carry on their business of providing telephone service--they purchase, install and maintain the necessary facilities, acquire other necessary properties and make arrangements for ongoing research and development in order to incorporate the latest innovations in providing the most efficient service at the lowest cost to the ratepayer. The patents that ensue from this research are the property of the AT&T Company.

The courts have affirmed that the ratepayer pays for service and has no ownership interest in the property acquired by the Operating Company. In Board of Public Utilities Commissioners et al. v. New York Telephone Company, 271 U.S. 23 (1926), the U.S. Supreme Court considered the rights of monopoly ratepayers to have the telephone company's depreciation reserves used to reduce the rates charged for service. The Court stated:

> "The revenue paid by the customer for service belongs to the company. . . . Customers pay for service, not for property used to render it. . . . By paying bills for service they do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company. Property paid for out of monies received for service belongs to the company. . . ."

Philadelphia Suburban Water Company v. Pennsylvania Public Utilities Commission, 427 Atl. 2d 1244 (1981), quoted Board of Public Commissioners v. New York Telephone Company with approval.

13. (continued) How many patents can be expected to result from research work currently in progress?

There is no way to predict the number of patents that will issue from any research work.

14. After the proposed settlement is approved, will AT&T license its pre-settlement patents on a nondiscriminatory basis to any applicant willing to pay reasonable royalties?

ANSWER As of April 1, 1982, AT&T was party to approximately 700 Patent License Agreements with more than 600 companies throughout the world, including most of the major manufacturers of telecommunications equipment such as IT&T, GTE, Nippon Electric, Northern Electric and Stromberg Carlson. Under most of these agreements, the patents so licensed include patents issuing on inventions made during the period 5 years after the effective dates of the agreements. With respect to agreements that became effective January 1, 1982, all Bell patents issuing on inventions made through December 31, 1986 (i.e., patents issuing well into 1989) are licensed for the lives of those patents. We have no reason to believe that such patents will not continue to be broadly licensed, in the same way as other companies determine how their intellectual property can best be used.

14. (continued) Will AT&T license its post-settlement patents on a nondiscriminatory basis to any applicant willing to pay reasonable royalties?

ANSWER Beyond the patents licensed pursuant to terms of the Patent License Agreements discussed above, we expect to act after divestiture in a commercially reasonable manner like any other commercial enterprise, including patent licensing.

15. After the proposed settlement is implemented, will design standards for the network and equipment connected thereto be established by AT&T, or by the BOCs? Specifically, who will set the standards for switched network services? For private line services? For digital services?

ANSWER With respect to network and service standards, AT&T will design for its operations and activities. We would expect that other intercity carriers, as well as the BOCs, will design for theirs. We would also expect that existing coordinating mechanisms such as USITA committees which have helped establish standards for network interconnection, will continue to serve that function.

With respect to "equipment connected thereto", the marketplace will determine what equipment is to be designed and used.

16. Under the proposed settlement, AT&T will retain its control of the network and its dominance of the terminal equipment market.

ANSWER The premises of the question are wrong. First, AT&T does not have "dominance" over the terminal equipment market. In fact, it's one of the most hotly competitive telecommunications marketplaces today. Competitors now win out 50 percent of the time in head-to-head PBX competition with AT&T - and half of the wins go to foreign companies. In Key Telephone Systems competitors win 70 percent of the time - and, again half the losses are to foreign companies.

Second, as to the network, many competing organizations are building alternative facilities using terrestrial microwave and satellites in direct competition with the telephone industry. By and large these facilities totally bypass AT&T's interexchange network.

With more satellites under construction and scheduled for launching in the next few years, and improved technology, this country's domestic satellite channel capacity will increase by 1986 to over one million equivalent voice channels--more than double the total Bell System long distance network capacity today. Bell will own only a small fraction of the 1986 satellite capacity.

Also a factor in the total long distance market are privately owned microwave systems. Today they number over 1,500, spanning over a quarter of a million route miles - a network more extensive than the Bell System's.

16. (continued) If AT&T designs the network or terminal equipment around a patent that it has no obligation to license, do you believe independent manufacturers will be hindered in their ability to manufacture equivalent or compatible equipment?

ANSWER AT&T does not "design the network" "around a patent." In fact, it is in our interest to have the widest possible use of network services consistent with sound network engineering practices. As to terminal equipment, the market is highly competitive, filled with high-technology domestic and foreign competitors. Consequently, AT&T should be able to design and patent freely and protect its patents and technology just as all of its competitors will be doing.

17. What are AT&T's intentions concerning the consolidation of control over SNET and CBI and the purchase of independent telephone companies?

ANSWER AT&T presently owns approximately 21% of the stock of SNET and 31% of the stock of CBI. There is no intention to acquire any additional stock in those companies nor does AT&T plan to purchase any of the other independent telephone companies.

18. What are the intentions of AT&T with respect to entering the digital termination systems and cellular radio markets?

ANSWER AT&T plans to expand its capabilities for digital transmission of information as quickly as is technologically and economically feasible.

With respect to cellular radio, AT&T plans to provide systems and equipment to the Bell Operating Companies and perhaps to other organizations. The local operating companies plan to offer cellular exchange services.

19. Since the BOCs will be restricted to the provision of access lines or access service from the customer premises of AT&T switching locations for connection to AT&T's interexchange services, will decisions as to what equipment will be located on the customers' premises and connected to such services be made by AT&T or by the BOCs?

ANSWER Essentially, the location of equipment on the customer premises is the customer's decision. Obviously, whichever company--the local operating company or any other company--directly terminates a service on the customer's premises may have need for equipment to be located on the premises. Under the Modification of Final Judgment, the local BOC can locate equipment on the customer's premises that is necessary to terminate its local exchange or exchange access services.

19. (continued) Will it be AT&T or the BOCs that provides any telephone company-provided equipment at the customers' premises for connection to the access lines? To AT&T's services?

ANSWER As a general matter, if AT&T equipment must be placed on a customer's premises to terminate an AT&T service on the premises, AT&T would do so. The same would be true of BOC equipment for services provided by the BOCs.

20. Will the BOCs be participating with AT&T in the provision of joint services (where the BOCs provide the local access) or will they merely be providing access to those AT&T-provided services?

ANSWER The modified Final Judgment requires the BOCs, assuming that they are at the ends of an AT&T-provided interexchange call, to file tariffs for access at each end as discrete and separate elements. The regulators, whose jurisdiction is essentially unchanged by the Modified Final Judgment, will determine whether and how "joint services" will be provided.

20. (continued) Will independent telephone companies cease to provide joint services and instead provide access service?

ANSWER The Modified Final Judgment does not govern the independent telephone companies. The question of whether independents will provide services should be directed to them. As Bell System plans to comply with the Modified Final Judgment evolve, we will work with the independent telephone companies with respect to the matters in which they have an interest.

20. (continued) What will be the consequences of such a change for the provision of customer-premises equipment?

ANSWER None, except the withdrawal of customer premises equipment from the base for determining separations and settlements, an issue which is not part of the Modification of Final Judgment, but which the FCC is currently dealing with in Docket No. 20981.

Statement of

HOWARD J. TRIENENS

My name is Howard J. Trienens. I am Vice President and General Counsel of the American Telephone and Telegraph Company.

I am pleased to have this opportunity to appear before you to discuss the modification of the 1956 Consent Decree by the entering of a new Consent Decree, and the dismissal of the 1974 case.

As discussed more fully in Mr. Tanenbaum's statement, the keystone of our agreement with the Department of Justice was the removal of the anticompetitive provisions of the 1956 Consent Decree which resolved the government suit instituted in 1949. These restrictions, which made sense in 1956, were becoming increasingly burdensome as the line between communications and data processing became less and less realistic. Removal of the restrictions of the 1956 Consent Decree could only be obtained by modification of that Consent Decree, which was under the jurisdiction of the United States District Court for the District of New Jersey.

On January 8, 1982, the parties filed a Modification of Final Judgment (Exhibit 1), a Stipulation of the Parties Consenting to the Modification (Exhibit 2), and a Memorandum in Connection with Stipulation and Modification of Final Judgment (Exhibit 3) with the New Jersey Court.

Simultaneously, the Department of Justice submitted to the Honorable Vincent P. Biunno, United States District Judge for the District of New Jersey, a Notice of Motion and Motion to Transfer this Cause to the United States District Court for the District of Columbia (Exhibit 4). The

American Telephone and Telegraph Company and Western Electric Company, Incorporated (defendants in the 1949 case) joined in the Motion to Transfer to the United States District Court for the District of Columbia (Exhibit 5). A Memorandum in Support of the Motion to Transfer to the District of Columbia (Exhibit 6), a Motion for Expedited Consideration of Motion to Transfer (Exhibit 7), and a suggested Order (Exhibit 8) were also filed at that time. These pleadings were intended to transfer jurisdiction of the 1956 Decree and the proposed Modification to the United States District Court for the District of Columbia in order to permit review by Judge Harold H. Greene, U.S.D.J.

At the time of the filing of the Modification of Final Judgment, an ancillary appeal by the Department of Justice of an interpretative ruling concerning the 1956 Decree was pending in the Third Circuit Court of Appeals. Because the 1956 Decree was being replaced totally by a new Decree, that appeal was moot and the parties filed with the Third Circuit a Joint Motion to Dismiss Appeals on Grounds of Mootness (Exhibit 9) and a Joint Motion for Expedited Consideration of Joint Motion to Dismiss Appeals (Exhibit 10).

Similarly, because the Modification of Final Judgment resolved all controversies between the United States and the Bell System, the parties filed a Stipulation for Voluntary Dismissal of the 1974 case (Exhibit 11) pursuant to Rule 41(a)(1)(ii) of the Federal Rules of Civil Procedure with the Clerk for the United States District Court for the District of Columbia.

After hearing counsel on January 11, Judge Biunno entered an Opinion (Exhibit 12) approving the Modification

of Final Judgment and reserving judgment on the request to transfer jurisdiction. Judge Biunno's decision to approve the proposed modification had not been sought by either party. In the transfer papers and at the hearing, the parties had sought transfer to the U.S. District Court for the District of Columbia in Washington to permit that Court to conduct appropriate proceedings prior to entry of the proposed modification of the 1956 Decree.

In pursuing these procedural steps, the parties followed the most appropriate course. Complications were inherent in the circumstance that there were two courts involved, one with a pending case and the other in which the 1956 Decree had been entered. Whether or not the Antitrust Procedures and Penalties Act of 1974 (the "Tunney Act") technically applies to a modification of the 1956 Consent Decree, both parties have from the very start contemplated that hearings permitting public comment and judicial review would be held and should be held in Washington, D.C. (as explicitly stated in the Memorandum in Connection with Stipulation and Modification of Final Judgment (Exhibit 3) filed jointly by the Department of Justice and AT&T on January 8, 1982).

On January 12, the parties appeared before Judge Harold H. Greene, U.S.D.J. in the District of Columbia, at his request. At that time Judge Greene indicated a concern with the procedural posture of the modification of the Consent Decree entered in 1956, and requested the parties to advise the Court not later than January 18 whether jurisdiction over the Consent Decree modification would be submitted to his court for application of Tunney Act procedures. On January 14, Judge Biunno entered an order

transferring jurisdiction to the United States District Court for the District of Columbia (Exhibit 13), and on January 18, the parties so notified Judge Greene pursuant to his request of January 12 (Exhibits 14 and 15). On January 20, Judge Biunno issued a Supplemental Opinion on his transfer order (Exhibit 16). On January 21, Judge Greene entered an Order setting forth in detail the procedures to be followed (Exhibit 17). These procedures track precisely the requirements of the Tunney Act and provide to all interested parties all of the procedural rights set forth in the Tunney Act.

Thus, procedures for public comment and review are now underway before Judge Greene. We have every confidence that Judge Greene will find the new decree to be in the public interest.

EXHIBIT 1

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA, Plaintiff	)	
v.	)	Civil Action No. 17-49
WESTERN ELECTRIC COMPANY, INCORPORATED, AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY, Defendants.	)	

MODIFICATION OF FINAL JUDGMENT

Plaintiff, United States of America, having filed its complaint herein on January 14, 1949; the defendants having appeared and filed their answer to such complaint denying the substantive allegations thereof; the parties, by their attorneys, having severally consented to a Final Judgment which was entered by the Court on January 24, 1956, and the parties having subsequently agreed that modification of such Final Judgment is required by the technological, economic and regulatory changes which have occurred since the entry of such Final Judgment;

Upon joint motion of the parties and after hearing by the Court, it is hereby

ORDERED, ADJUDGED, AND DECREED that the Final Judgment entered on January 24, 1956, is hereby vacated in its entirety and replaced by the following items and provisions:

I

AT&T Reorganization

A. Not later than six months after the effective date of this Modification of Final Judgment, Defendant AT&T shall submit to the Department of Justice for its approval, and thereafter implement, a plan of reorganization. Such plan shall provide for the completion, within 18 months after the effective date of this Modification of Final Judgment, of the following steps:

1. The transfer from AT&T and its affiliates to the BOCs, or to a new entity subsequently to be separated from AT&T and to be owned by the BOCs, of sufficient facilities, personnel, systems, and rights to technical information to permit the BOCs to perform, independently of AT&T, exchange telecommunications and exchange access functions, including the procurement for, and engineering, marketing and management of, those functions, and sufficient to enable the BOCs to meet the equal exchange access requirements of Appendix B;

2. The separation within the BOCs of all facilities, personnel and books of account between those relating to the exchange telecommunications or exchange access functions and those relating to other functions (including the provision of interexchange switching and transmission and the provision of customer premises equipment to the public); provided that there shall be no joint ownership of facilities, but appropriate provision may be made for sharing, through leasing or otherwise, of multifunction facilities so long as the separated portion of each BOC is ensured control over the exchange telecommunications and exchange access functions;

3. The termination of the License Contracts between AT&T and the BOCs and other subsidiaries and the Standard Supply Contract between Western Electric and the BOCs and other subsidiaries; and

4. The transfer of ownership of the separated portions of the BOCs providing local exchange and exchange access services from AT&T by means of a spin-off of stock of the separated BOCs to the shareholders of AT&T, or by other disposition; provided that nothing in this Modification of Final Judgment shall require or prohibit the consolidation of the ownership of the BOCs into any particular number of entities.

B. Notwithstanding separation of ownership, the BOCs may support and share the costs of a centralized organization for the provision of engineering, administrative and other services which can most efficiently be provided on a centralized basis. The BOCs shall provide, through a centralized organization, a single point of contact for coordination of BOCs to meet the requirements of

national security and emergency preparedness.

C. Until September 1, 1987, AT&T, Western Electric, and the Bell Telephone Laboratories, shall, upon order of any BOC, provide on a priority basis all research, development, manufacturing, and otner support services to enable the BOCs to fulfill the requirements of this Modification of Final Judgment. AT&T and its affiliates snall take no action that interferes with the BOCs' requirements of nondiscrimination established by section II.

D. After the reorganization specified in paragraph A(4), AT&T shall not acquire the stock or assets of any BOC.

II

BOC Requirements

A. Subject to Appendix B, each BOC shall provide to all interexchange carriers and information service providers exchange access, information access, and exchange services for such access on an unbundled, tariffed basis, that is equal in type, quality, and price to that provided to AT&T and its affiliates.

B. No BOC shall discriminate between AT&T and its affiliates and their products and services and other persons and their products and services in the:

1. procurement of products and services;

2. establishment and dissemination of technical information and procurement and interconnection standards;

3. interconnection and use of the BOC's telecommunications service and facilities or in the charges for each element of service; and

4. provision of new services and the planning for and implementation of the construction or modification of facilities, used to provide exchange access and information access.

C. Within six months after the reorganization specified in I(A)4, each BOC shall submit to the Department of Justice procedures for ensuring compliance with the requirements of paragraph B.

D. After completion of the reorganization specified in Section I, no BOC shall, directly or through any affiliated enterprise:

1. provide interexchange telecommunications services or information services;

2. manufacture or provide telecommunications products or customer premises equipment (except for provision of customer premises equipment for emergency services); or

3. provide any other product or service, except exchange telecommunications and exchange access service, that is not a natural monopoly service actually regulated by tariff.

III

Applicability and Effect

The provisions of this Modification of Final Judgment, applicable to each defendant and each BOC, shall be binding upon said defendants and BOCs, their affiliates, successors and assigns, officers, agents, servants, employees, and attorneys, and upon those persons in active concert or participation with each defendant and BOC who receives actual notice of this Modification of Final Judgment by personal service or otherwise. Each defendant and each person bound by the prior sentence shall cooperate in ensuring that the provisions of this Modification of Final Judgment are carried out. Neither this Modification of Final Judgment nor any of its terms or provisions shall constitute any evidence against, an admission by, or an estoppel against any party or BOC. The effective date of this Modification of Final Judgment shall be the date upon which it is entered.

IV

Definitions

For the purposes of this Modification of Final Judgment:

A. "Affiliate" means any organization or entity, including defendant Western Electric Company, Incorporated, and Bell Telephone Laboratories, Incorporated, that is under direct or indirect common ownership with or control by AT&T or is owned or controlled by another affiliate. For the purposes of this paragraph, the terms "ownership" and "owned" mean a direct or indirect equity interest (or the equivalent thereof) of more than fifty (50) percent of an entity. "Subsidiary" means any organization or entity in which AT&T has stock ownership, whether or not controlled by AT&T.

B. "AT&T" shall mean defendant American Telephone and Telegraph Company and its affiliates.

C. "Bell Operating Companies" and "BOCs" mean the corporations listed in Appendix A attached to this Modification of Final Judgment and any entity directly or indirectly owned or controlled by a BOC or affiliated through substantial common ownership.

D. "Carrier" means any person deemed a carrier under the Communications Act of 1934 or amendments thereto, or, with respect to intrastate telecommunications, under the laws of any state.

E. "Customer premises equipment" means equipment employed on the premises of a person (other than a carrier) to originate, route, or terminate telecommunications, but does not include equipment used to multiplex, maintain, or terminate access lines.

F. "Exchange access" means the provision of exchange services for the purpose of originating or terminating interexchange telecommunications. Exchange access services include any activity or function performed by a BOC in connection with the origination or termination of interexchange telecommunications, including but not limited to, the provision of network control signalling, answer supervision, automatic calling number identification, carrier access codes, directory services, testing and maintenance of facilities and the provision of information necessary to bill customers. Such services shall be provided by facilities in an exchange area for the transmission, switching, or routing, within the exchange area, of interexchange traffic originating or terminating within the exchange area, and shall include switching traffic within the exchange area above the end office and delivery and receipt of such traffic at a point or points within an exchange area designated by an interexchange carrier for the connection of its facilities with those of the BOC. Such connections, at the option of the interexchange carrier, shall deliver traffic with signal quality and characteristics equal to that provided similar traffic of AT&T, including equal probability of blocking, based on reasonable traffic estimates supplied by each interexchange carriers. Exchange services for exchange access shall not include the performance by any BOC of interexchange traffic routing for any interexchange

carrier. In the reorganization specified in section I, trunks used to transmit AT&T's traffic between end offices and class 4 switches shall be exchange access facilities to be owned by the BOCs.

G. "Exchange area," or "exchange" means a geographic area established by a BOC in accordance with the following criteria:

1. any such area shall encompass one or more contiguous local exchange areas serving common social, economic, and other purposes, even where such configuration transcends municipal or other local governmental boundaries;

2. every point served by a BOC within a State shall be included within an exchange area;

3. no such area which includes part or all of one standard metropolitan statistical area (or a consolidated statistical area, in the case of densely populated States) shall include a substantial part of any other standard metropolitan statistical area (or a consolidated statistical area, in the case of densely populated States), unless the Court shall otherwise allow; and

4. except with approval of the Court, no exchange area located in one State shall include any point located within another State.

H. "Information" means knowledge or intelligence represented by any form of writing, signs, signals, pictures, sounds, or other symbols.

I. "Information access" means the provision of specialized exchange telecommunications services by a BOC in an exchange area in connection with the origination, termination, transmission, switching, forwarding or routing of telecommunications traffic to or from the facilities of a provider of information services. Such specialized exchange telecommunications services include, where necessary, the provision of network control signalling, answer supervision, automatic calling number identification, carrier access codes, testing and maintenance of facilities, and the provision of information necessary to bill customers.

J. "Information service" means the offering of a capability for generating, acquiring, storing, transforming, processing,

retrieving, utilizing, or making available information which may be conveyed via telecommunications, except that such service does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.

K. "Interexchange telecommunications" means telecommunications between a point or points located in one exchange telecommunications area and a point or points located in one or more other exchange areas or a point outside an exchange area.

L. "Technical information" means intellectual property of all types, including, without limitation, patents, copyrights, and trade secrets, relating to planning documents, designs, specifications, standards, and practices and procedures, including employee training.

N. "Telecommunications equipment" means equipment, other than customer premises equipment, used by a carrier to provide telecommunications services.

O. "Telecommunications" means the transmissions, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received, by means of electromagnetic transmission, with or without benefit of any closed transmission medium, including all instrumentalities, facilities, apparatus, and services (including the collection, storage, forwarding, switching, and delivery of such information) essential to such transmission.

P. "Telecommunications service" means the offering for hire of telecommunications facilities, or of telecommunications by means of such facilities.

Q. "Transmission facilities" means equipment (including without limitation wire, cable, microwave, satellite, and fibre-optics) that transmit information by electromagnetic means or which directly support such transmission, but does.not include customer-premises equipment.

V

Compliance Provisions

Tne defendants, each BOC, and affiliated entities are ordered and directed to advise their officers and other management personnel with significant responsibility for matters addressed in this Modification of Final Judgment of their obligations hereunder. Each BOC shall undertake the following with respect to each such officer or management employee:

1. The distribution to them of a written directive setting forth their employer's policy regarding compliance with the Sherman Act and with this Modification of Final Judgment, with such directive to include:

(a) an admonition that non-compliance with such policy and this Modification of Final Judgment will result in appropriate disciplinary action determined by their employer and which may include dismissal; and

(b) advice that the BOCs' legal advisors are available at all reasonable times to confer with such persons regarding any compliance questions or problems

2. The imposition of a requirement that each of them sign and submit to their employer a certificate in substantially the following form:

> The undersigned hereby (1) acknowledges receipt of a copy of the 1982 United States v. Western Electric, Modification of Final Judgment and a written directive setting forth Company policy regarding compliance with the antitrust laws and with such Modification of Final Judgment, (2) represents that the undersigned has read such Modification of Final Judgment and directive and understands those provisions for which the undersigned has responsibility, (3) acknowledges that the undersigned has been advised and understands that non-compliance with such policy and Modification of Final Judgment will result in appropriate disciplinary measures determined by the Company and which may include dismissal, and (4) acknowledges that the undersigned has been advised and understands that non-compliance with the Modification of Final Judgment may also result in conviction for contempt of court and imprisonment and/or fine.

VI

Visitorial Provisions

A. For the purpose of determining or securing compliance with

this Modification of Final Judgment, and subject to any legally recognized privilege, from time to time:

1. Upon written request of the Attorney General or of the Assistant Attorney General in charge of the Antitrust Division, and on reasonable notice to a defendant or after the reorganization specified in Section I, a BOC, made to its principal office, duly authorized representatives of the Department of Justice shall be permitted access during office hours of such defendants or BOCs to depose or interview officers, employees, or agents, and inspect and copy all books, ledgers, accounts, correspondence, memoranda and other records and documents in the possession or under the control of such defendant, BOC, or subsidiary companies, who may have counsel present, relating to any matters contained in this Modification of Final Judgment; and

2. Upon the written request of the Attorney General or of the Assistant Attorney General in charge of the Antitrust Division made to a defendant's principal office or, after the reorganization specified in Section I, a BOC, such defendant, or BOC, shall submit such written reports, under oath if requested, with respect to any of the matters contained in this Modification of Final Judgment as may be requested.

B. No information or documents obtained by the means provided in this Section shall be divulged by any representative of the Department of Justice to any person other than a duly authorized representative of the Executive Branch of the United States or the Federal Communications Commission, except in the course of legal proceedings to which the United States is a party, or for the purpose of securing compliance with this Final Judgment, or as otherwise required by law.

C. If at the time information or documents are furnished by a defendant to a plaintiff, such defendant or a BOC represents and identifies in writing the material in any such information or documents to which a claim of protection may be asserted under

Rule 26(c)(7) of the Federal Rules of Civil Procedure, and said defendant or BOC marks each pertinent page of such material, "Subject to claim of protection under Rule 26(c)(7) of the Federal Rules of Civil Procedure," then 10 days' notice shall be given by plaintiff to such defendant or BOC prior to divulging such material in any legal proceeding (other than a grand jury proceeding) to which that defendant BOC is not a party.

VII

Retention of Jurisdiction

Jurisdiction is retained by this Court for the purpose of enabling any of the parties to this Modification of Final Judgment, or, after the reorganization specified in Section I, a BOC to apply to this Court at any time for such further orders or directions as may be necessary or appropriate for the construction or carrying out of this Modification of Final Judgment, for the modification of any of the provisions hereof, for the enforcement of compliance herewith, and for the punishment of any violation hereof.

Entered this _____day of _____, 1982.

_____

United States District Judge

APPENDIX A

Bell Telephone Company of Nevada
Illinois Bell Telephone Company
Indiana Bell Telephone Company, Incorporated
Michigan Bell Telephone Company
New England Telephone and Telegraph Company
New Jersey Bell Telephone Company
New York Telephone Company
Northwestern Bell Telephone Company
Pacific Northwest Bell Telephone Company
South Central Bell Telephone Company
Southern Bell Telephone and Telegraph Company
Southwestern Bell Telephone Company
The Bell Telephone Company of Pennsylvania
The Chesapeake and Potomac Telephone Company
The Chesapeake and Potomac Telephone Company of Maryland
The Chesapeake and Potomac Telephone Company of Virginia
The Chesapeake and Potomac Telephone Company of West Virginia
The Diamond State Telephone Company
The Mountain States Telephone and Telegraph Company
The Ohio Bell Telephone Company
The Pacific Telephone and Telegraph Company
Wisconsin Telephone Company

APPENDIX B

PHASED-IN BOC PROVISION OF EQUAL EXCHANGE ACCESS

A. 1. As part of its obligation to provide non-discriminatory access to interexchange carriers, no later than September 1, 1984, each BOC shall begin to offer to all interexchange carriers exchange access on an unbundled, tariffed basis, that is equal in type and quality to that provided for the interexchange telecommunications services of AT&T and its affiliates. No later than September 1, 1985, such equal access shall be offered through end offices of each BOC serving at least one-third of that BOC's exchange access lines and, upon bona fide request, every end office shall offer such access by September 1, 1986. Nothing in this Modification of Final Judgment shall be construed to permit a BOC to refuse to provide to any interexchange carrier or information service provider, upon bona fide request, exchange or information access superior or inferior in type or quality to that provided for AT&T's interexchange services or information services at charges reflecting the reduced or increased cost of such access.

2. (i) Notwithstanding paragraph (1), in those instances in which a BOC is providing exchange access for Message Telecommunications Service on the effective date of this

modification of Final Judgment through access codes that do not permit the designation of more than one interexchange carrier, then, in accordance with the schedule set out in paragraph (1), exchange access for additional carriers shall be provided through access codes containing the minimum number of digits necessary at the time access is sought to permit nationwide, multiple carrier designation for the number of interexchange carriers reasonably expected to require such designation in the immediate future.

(ii) Each BOC shall, in accordance with the schedule set out in paragraph (1), offer as a tariffed service exchange access that permits each subscriber automatically to route, without tne use of access codes, all the subscriber's interexchange communications to the interexchange carrier of the customer's designation.

(iii) At such time as the national numbering area (area code) plan is revised to require the use of additional digits, each BOC shall provide exchange access to every interexchange carrier, including AT&T, through a uniform number of digits.

3. Notwithstanding paragraphs (1) and (2), with respect to access provided through an end office employing switches technologically antecedent to electronic, stored program control switches or those offices served by switches that characteristically serve fewer than 10,000 access lines, a BOC may not be required to provide equal access through a switch if, upon complaint being made to the Court, the BOC carries the burden of showing that for particular categories of services such access is not physically feasible except at costs that clearly outweigh potential benefits to users of telecommunications services. Any such denial of access under the preceding sentence shall be for the minimum divergence in access necessary, and for the minimum time necessary, to achieve such feasibility.

B. 1. The BOCs are ordered and directed to file, to become effective on the effective date of the reorganization described in I(A)(4), tariffs for the provision of exchange access including the

provision by each BOC of exchange access for AT&T's interexchange telecommunications. Such tariffs shall provide unbundled schedules of charges for exchange access and shall not discriminate against any carrier or other customer. Such tariffs shall replace the division of revenues process used to allocate revenues to a BOC for exchange access provided for the interexchange telecommunications of BOCs or AT&T.

2. Each tariff for exchange access shall be filed on an unbundled basis specifying each type of service, element by element, and no tariff shall require an interexchange carrier to pay for types of exchange access that it does not utilize. The charges for each type of excnange access shall be cost justified and any differences in charges to carriers shall be cost justified on the basis of differences in services provided.

3. Notwithstanding the requirements of paragraph 2, from tne date of reorganization specified in section I until September 1, 1991, the charges for delivery or receipt of traffic of the same type between end offices and facilities of interexchange carriers within an exchange area, or within reasonable subzones of an exchange area, shall be equal, per unit of traffic delivered or received, for all interexchange carriers; provided, that the facilities of any interexchange carrier within five miles of an AT&T class 4 switch shall, with respect to end offices served by such class 4 switch, be considered to be in the same subzone as such class 4 switch.

4. Each BOC offering exchange access as part of a joint or through service shall offer to make exchange access available to all interexchange carriers on the same terms and conditions, and at the same charges, as are provided as part of a joint or through service, and no payment or consideration of any kind shall be retained by the BOC for the provision of exchange access under such joint or through service other than through tariffs filed pursuant to this paragraph.

C. 1. Nothing in this Modification of Final Judgment shall be construed to require a BOC to allow joint ownership or use of its switches, or to require a BOC to allow co-location in its building of the equipment of other carriers. When a BOC uses facilities that

(i) are employed to provide exchange telecommunications or exchange access or both, and (ii) are also used for the transmission or switching of interexchange telecommunications, then the costs of such latter use shall be allocated to the interexchange use and shall be excluded from the costs underlying the determination of charges for either of the former uses.

2. Nothing in this Modification of Final Judgment shall either require a BOC to bill customers for the interexchange services of any interexchange carrier or preclude a BOC from billing its customers for the interexchange services of any interexchange carrier it designates, provided that when a BOC does provide billing services to an interexchange carrier, the BOC may not discontinue local exchange service to any customer because of nonpayment of interexchange charges unless it offers to provide billing services to all interexchange carriers, and provided further that the BOC's cost of any such billing shall be included in its tariffed access charges to that interexchange carrier.

3. Whenever, as permitted by this Modification of Final Judgment, a BOC fails to offer exchange access to an interexchange carrier that is equal in type and quality to that provided for the interexchange traffic of AT&T, nothing in this Modification of Final Judgment shall prohibit the BOC from collecting reduced charges for such less-than-equal exchange access to reflect the lesser value of such exchange access to the interexchange carrier and its customers compared to the exchange access provided AT&T.

EXHIBIT 2

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Civil Action
	)	No. 17-49
WESTERN ELECTRIC COMPANY, INCORPORATED, AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	
	)	
Defendants.	)	

STIPULATION

It is stipulated by and between the undersigned parties, Plaintiff, United States of America, and Defendants, American Telephone & Telegrapn Company and Western Electric Company, Incorporated, by their respective attorneys, that:

1. The parties consent that a Modification of Final Judgment in the form hereto attached may be filed and entered by the Court, upon the motion of any party or upon the Court's own motion, at any time after hearing by the Court and without further notice to any party or other proceedings, provided that Plaintiff has not withdrawn its consent, which it may do at any time before the entry of the proposed Final Judgment by serving notice thereof on Defendants and by filing that notice with the Court.

2. In the event Plaintiff withdraws its consent or if the proposed Modification of Final Judgment is not entered pursuant to this Stipulation, this Stipulation shall be of no effect

whatever and the making of this Stipulation shall be without prejudice to Plaintiff or Defendants in this or any other proceeding.

Dated: January 8, 1982

FOR THE PLAINTIFF:

William F. Baxter

WILLIAM F. BAXTER
Assistant Attorney General
Antitrust Division
Department of Justice
Washington, D.C. 20530

FOR THE DEFENDANTS:

Howard J. Trienens

HOWARD J. TRIENENS
Vice President and General Counsel
for American Telephone and
Telegraph Company
195 Broadway
New York, New York 10007

EXHIBIT 3

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Civil Action No. 17-49
	)	
WESTERN ELECTRIC COMPANY, INCORPORATED and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	
	)	
Defendants.	)	

MEMORANDUM IN CONNECTION WITH STIPULATION
AND MODIFICATION OF FINAL JUDGMENT

Plaintiff and Defendants are filing this Memorandum in order to inform the Court of the procedures that they believe appropriate to facilitate judicial consideration of the Stipulated Modification of Final Judgment filed today.

A court presented with an agreed-upon modification to an antitrust consent decree may, under its general equitable powers, employ procedures appropriately designed to assure that the agreed-upon modification is in the public interest. See United States v. Swift & Co., 1975-1 Trade Cases ¶ 60,201 (N.D. Ill. 1975). The parties believe that, with respect to a modification of final judgment as important as that at hand, the kinds of procedures required for proposed antitrust consent judgments by the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16, provide useful ways both of assuring public notification and fully explicating the modification's effects on competition.

Accordingly, upon transfer of this case to the United States District Court for the District of Columbia, Plaintiff intends to publish in the Federal Register the agreed-upon Modification of Final Judgment. Plaintiff shall also endeavor, as soon thereafter as is practicable, to file and publish in the Federal Register a statement describing the Modification and its likely impact on competition.

Dated: January 8, 1982

FOR THE PLAINTIFF:

William F. Baxter

WILLIAM F. BAXTER
Assistant Attorney General
Antitrust Division
Department of Justice
Washington, D.C. 20430

FOR THE DEFENDANTS:

Howard J. Trienens

HOWARD J. TRIENENS
Vice President and General Counsel
for American Telephone and
Telegraph Company
195 Broadway
New York, New York 10007

EXHIBIT 4

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA,	)	THE HONORABLE VINCENT P. BIUNNO
	)	
Plaintiff,	)	Civil Action No. 17-49
v.	)	
	)	
WESTERN ELECTRIC COMPANY, INCORPORATED, and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	NOTICE OF MOTION AND MOTION TO TRANSFER THIS CAUSE TO THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA
	)	
Defendants.	)	

TO: S. JOSEPH FORTUNATO
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Morristown, New Jersey 07960

HOWARD J. TRIENENS
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and Telegraph Company
195 Broadway
New York, New York 10007

GEORGE V. COOK
Vice President and General
Counsel for Western Electtic
Company, Incorporated
222 Broadway
New York, New York 10038

PLEASE TAKE NOTICE tnat on February 5, 1982 or the earliest date established by the Court, the undersigned attorneys for plaintiff, the United States, will move before The Honorable Vincent P. Biunno, United States District Court for the District of New Jersey, at the United States Courthouse and Post Office Building, Newark, New Jersey, that this cause be transferred to the United States District Court for the District of Columbia. In support of its

motion, plaintiff states that defendants have joined in this motion and agree with plaintiff that transfer will serve the convenience of the parties and the interests of justice. In further support of its motion, plaintiff submits the accompanying Memorandum in Support of Motion To Transfer.

January 8, 1982

Respectfully submitted,

WILLIAM F. BAXTER
Assistant Attorney General

RONALD G. CARR
Deputy Assistant Attorney General

Attorneys for the United States
Department of Justice
Washington, D.C. 20530

EXHIBIT 5

ORIGINAL FILED
JAN 8 1982
ANGELO W. LOCASCIO, CLERK

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA, Plaintiff,	)	
v.	)	Civil Action No. 17-49
WESTERN ELECTRIC COMPANY, INCORPORATED, and AMERICAN TELEPHONE AND TELEGRAPH COMPANY, Defendants.	)	

Defendants, Western Electric Company, Incorporated, and American Telephone and Telegraph Company, hereby join in the Motion To Transfer This Cause To The United States District Court for the District of Columbia filed this 8th day of January, 1982, by Plaintiff, United States, and in the Motion for Expedited Consideration of said motion also filed today.

S. Joseph Fortunato

S. JOSEPH FORTUNATO
Pitney, Hardin, Kipp & Szuch
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HOWARD J. TRIENENS
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GEORGE V. COOK
Vice President and General
Counsel for Western Electric
Company, Incorporated
222 Broadway
New York, New York 10038

Dated: January 8, 1982

EXHIBIT 6

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA,	)	
	)	
Plaintiff,	)	THE HONORABLE VINCENT P. BIUNNO
	)	
vs.	)	
	)	Civil Action No. 17-49
WESTERN ELECTRIC COMPANY, INCORPORATED and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	
	)	
Defendants.	)	

MEMORANDUM IN SUPPORT OF THE MOTION TO TRANSFER TO THE DISTRICT OF COLUMBIA

Pursuant to 28 U.S.C. §1404(a), plaintiff, the United States has moved to transfer this case to the United States District Court for the District of Columbia. Defendants ("AT&T") have joined in that motion. A related antitrust action has been pending between the parties in the District of Columbia. United States v. American Telephone and Telegraph Co., et al., No. 74-1698 (D.D.C.). Transfer of this case will serve the convenience of the parties and the interests of justice and promote a comprehensive resolution of the antitrust controversies between AT&T and the United States. This memorandum is submitted in support of the motion to transfer.

Preliminary Statement

The United States instituted this action against AT&T in 1949. The complaint alleged that defendants had violated the Sherman Act and requested structural relief, including the divestiture of Western Electric Co. by AT&T. Final judgment was entered, by consent of the parties, on January 24, 1956 ("1956 Consent Decree"). The Decree retains jurisdiction in

this Court to allow any of the parties to apply at any time for construction, modification, or termination of any of the provisions of the Decree (Section XVII).

In 1974, the United States filed, in the District of Columbia, another action under the Sherman Act against AT&T. United States v. American Telephone and Telegraph Co., et al., No. 74-1698 (D.D.C.). In that action, the United States alleged violations of the Sherman Act and sought substantial structural relief. Following extensive pretrial proceedings, the trial in the District of Columbia suit began on January 15, 1981, and testimony commenced on March 4, 1981. The trial was recessed on December 18, 1981 and had been scheduled to resume on January 12, 1982. The record that has been compiled includes over 24,000 transcript pages and voluminous exhibits.

On December 31, 1981, the United States and AT&T announced that they were conducting discussions designed to produce a comprehensive resolution of the antitrust controversies between them. As of today's date, the United States and AT&T have agreed on such a resolution in the form of a modification of the 1956 Consent Decree.

Simultaneously with the filing of this motion, the United States and AT&T have voluntarily dismissed without prejudice the District of Columbia suit pursuant to Fed. R. Civ. P. 41(a) and have filed, in this Court, the proposed modification of the 1956 Consent Decree. This motion to transfer has been filed by plaintiff and joined in by defendants, who agree that it would promote the convenience of the parties and the interests of justice to have the proceedings relating to the modification of tne 1956 Consent Decree take place in the United States District Court for the District of Columbia.

Argument

The motion to transfer is based on 28 U.S.C. §1404(a), which provides as follows:

> "For the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought."

Pursuant to this section, antitrust actions have been transferred to other Districts after the entry of consent decrees, even where -- as is not the case here -- one of the parties opposed the transfer. United States v. Swift & Co., 158 F.Supp. 551 (D.D.C. 1958)(transferring 1920 Meat Packers Decree to Illinois over the objection of the United States); see also United States v. National City Lines, Inc., 337 U.S. 78 (1949) (§1404 applies to civil antitrust actions brought by the United States). Commentators have approved these holdings. 1 Moore's Federal Practice ¶¶ 0.145[4.-1], 0.145[4.-3] (2nd ed. 1981); see 15 Wright, Miller & Cooper, Federal Practice and Procedure, §3844 p. 212 (1976).

In this case, all of the parties favor transfer. This, by itself, should be dispositive. At least one federal appellate court has indicated that an action may be transferred where all parties consent to a transfer or alternatively if the requirements of §1404(a) have been met. International Telephone and Telegraph Corp. v. General Telephone and Electronics Corp. 527 F.2d 1162, 1164 (4th Cir. 1975). In any event, in this instance, it is manifest that transfer will satisfy all the requirements of §1404(a).

A. Transfer Will Promote the Convenience of the Parties

A principal factor to be considered in evaluating any transfer

motion is the convenience of the parties. It is the parties who must bear the burden of litigation and of the administration of any decree. See Grubs v. Consolidated Freightways, Inc., 189 F.Supp. 404 (D.Mont. 1960). In the typical case in which a §1404(a) motion is filed, it is clear that some party will be inconvenienced "whether the case be transferred or retained in this jurisdiction." United States v. Swift & Co., supra, 158 F.Supp. at 558. As a consequence, the decision whether to transfer is ordinarily made by balancing the convenience to one party against the inconvenience to the other. Willetts v. General Telephone Directory Co., 38 F.R.D. 406 (S.D.N.Y. 1965). Here, in contrast, no balancing is required. The parties agree that their mutual convenience requires the transfer of this case to the District of Columbia.

In any event, there can be no question that transferring this case to the District of Columbia will in fact promote the convenience of both the United States and AT&T. The District of Columbia is the most convenient forum for the parties. The Antitrust Division of the Department of Justice is located in that District. AT&T has major offices in the District of Columbia, both because it is the Nation's Capital and because the federal agencies that regulate AT&T and shape national communications policy -- the Federal Communications Commission and the National Telecommunications and Information Administration -- are located there. For these reasons, the District of Columbia has been the focal point of the antitrust and antitrust-related controversies between the parties over the past decade and has, of course, been the District in which the extensive proceedings in United States v. AT&T have occurred.

That the voluminous litigation in United States v. AT&T has been in progress in the District of Columbia is the clearest indication that it is the most convenient forum for the

proceedings relating to the modification of the 1956 Consent Decree. The District of Columbia suit and this action are related in many respects. Where related complex litigation is occurring in the transferee district, federal courts have uniformly ordered transfer to promote the parties' convenience. See, e.g., Impervious Paint Industries, Ltd. v. Ashland Oil, Inc., 444 F.Supp. 465 (E.D.Pa. 1978); Wyndham Associates v. Bintliff, 398 F.2d 614 (2d Cir.), cert. denied, 393 U.S. 977 (1968). Here, over seven years of pretrial proceedings and approximately nine months of trial have taken place in a related suit in the transferee forum.

B. Transfer Will Promote The Interest of Justice

The second important factor in a §1404(a) motion for transfer is the interest of justice. Transferring this case to the District of Columbia manifestly will promote judicial efficiency and the interest of justice. For most of the past year, the Court in the District of Columbia has presided over a massive trial involving complex issues relating to current antitrust controversies between the parties. Although that case is today being dismissed without prejudice by agreement of the parties, the enormous efforts of the parties and Court in that case will be of great value in the proceedings relating to the modification of the 1956 Consent Decree, filed today. Transfer will plainly serve the interests of justice.

C. This Action Might have Been Brought In The District of Columbia

Finally, this Court plainly has the power to transfer this action pursuant to §1404(a) because this suit "might have been brought" in the District of Columbia. Under 15 U.S.C. §22, a action by the United States under the Sherman Act can be

brought in any district in which the defendant corporation "may be found or transacts business." Both defendant AT&T and defendant Western Electric Co. "may be found or transact[] business" in the District of Columbia -- as is evidenced by the fact that United States v. AT&T, No. 74-1698 (D.D.C.), was filed in that District.

Conclusion

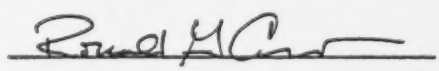
For the reasons stated, this cause should be transferred to the United States District Court for the District of Columbia.

January 8, 1982

Respectfully submitted,

WILLIAM F. BAXTER
Assistant Attorney General

RONALD G. CARR
Deputy Assistant Attorney General



Attorneys for the United States
United States Department of Justice
Washington, DC 20530

EXHIBIT 7

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA,	)	
	)	
Plaintiff,	)	THE HONORABLE VINCENT P. BIUNNO
	)	
vs.	)	
	)	Civil Action No. 17-49
WESTERN ELECTRIC COMPANY, INCORPORATED and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	
	)	
Defendants.	)	

MOTION FOR EXPEDITED CONSIDERATION
OF MOTION TO TRANSFER

Plaintiff hereby moves for expedited consideration of its motion to transfer this cause to the United States District Court for the District of Columbia. Defendants ("AT&T") have joined both in Plaintiff's motion to transfer and in this motion for expedited consideration. Plaintiff requests that the parties be heard on the motion to transfer on January 8, 1982, or as soon thereafter as counsel may be heard.

Transfer of this case to the District of Columbia at this time is clearly warranted under 28 U.S.C. §1404(a). That transfer will be for the convenience of the parties and in the interest of justice is manifest. No party to this case disagrees with this conclusion. All parties agree that the case should be transferred forthwith; no party is in need or want of further opportunity to consider or raise possible objections to transfer.

AT&T and the United States greatly wish to eliminate any unnecessary delay in the resolution of the antitrust controversies between them. Expeditious resolution of these controversies is of great moment to the parties; steps have already been taken to achieve it, and the parties are most anxious to begin the final stage of the process -- actual consideration of their proposed modification of the 1956 Consent Decree.

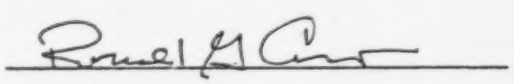
In these circumstances, Plaintiff respectfully requests expedited consideration of the motion to transfer.

January 8, 1982

Respectfully submitted,

WILLIAM F. BAXTER
Assistant Attorney General

RONALD G. CARR
Deputy Assistant Attorney General



Attorneys for the United States
Department of Justice
Washington, D.C. 20530

EXHIBIT 8

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA,	)	
	)	
Plaintiff,	)	
v.	)	THE HONORABLE VINCENT P. BIUNNO
	)	
WESTERN ELECTRIC COMPANY, INCORPORATED and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	CIVIL ACTION NO. 17-49
	)	
Defendants.	)	

ORDER

This matter having come before the Court on the motion of plaintiff, tne United States, to transfer this cause to the United States District Court for the District of Columbia pursuant to 28 U.S.C. § 1404(a), defendants having joined in this motion, and this Court having reviewed the memorandum of the United States, this Court

FINDS that the requirements of 28 U.S.C. § 1404(a) have been satisfied, and

IT IS HEREBY ORDERED that this cause is transferred to the United States District Court for the District of Columbia pursuant to 28 U.S.C. § 1404(a).

Date: _____

_____
United States District Judge

The parties hereby consent to the form of this Order.

_____
Ronald G. Carr
Deputy Assistant Attorney General
Antitrust Division
Department of Justice
Washington, D.C. 20530
Attorney for Plaintiff

_____
S. Joseph Fortunato
Pitney, Hardin, Kipp & Szuch
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Morristown, New Jersey 07960
Attorney for Defendants

EXHIBIT 9

IN THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

UNITED STATES OF AMERICA, Plaintiff-Appellee, v. WESTERN ELECTRIC CO. and AMERICAN TELEPHONE AND TELEGRAPH CO., Defendants-Appellees; ALARM INDUSTRY TELECOMMUNICATIONS COMMITTEE, ET AL., Proposed Intervenors-Appellants.	Nos. 81-1960 and consolidated cases
UNITED STATES OF AMERICA, Plaintiff-Appellant, v. WESTERN ELECTRIC CO. and AMERICAN TELEPHONE AND TELEGRAPH CO., Defendants-Appellees.	No. 81-2837

JOINT MOTION OF UNITED STATES AND AT&T TO DISMISS APPEALS ON GROUNDS OF MOOTNESS

Plaintiff-appellant United States of America and Defendants-appellees Western Electric Company and American Telephone and Telegraph (collectively, "AT&T") hereby move this

Court to dismiss as moot Case No. 81-2837, the appeal by the United States from the order of the district court granting AT&T's motion for construction of the consent decree entered in this case -- United States v. Western Electric Co. -- in 1956 (the "merits appeal"). The United States and AT&T also move this Court to dismiss as moot Case Nos. 81-1960 et al., all of which are appeals from the district court's denial of various motions to intervene in the decree construction proceeding (the "intervention appeals"). The grounds for this motion are as follows.

The present litigation began in March 1981 when AT&T filed a motion for construction of the 1956 decree. The United States opposed the motion. A number of persons sought unsuccessfully to intervene in the proceedings; some of these now have appeals pending in this Court from the denial of intervention. 1/

The district court granted AT&T's motion for construction, and the United States appealed. By order dated December 29, 1981, this Court consolidated for briefing and argument the merits appeal and the intervention appeals. It also denied

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1/ Three proposed intervenors also filed separate "protective" notices of appeal from the district court's decision on the merits, conditioned on their obtaining a reversal of the denial of intervention. Since the merits appeal and the intervention appeals have become moot, these "protective" appeals (Nos. 81-2929, 81-2930, and 81-2998) are also moot and should be dismissed.

motions by some proposed intervenors to intervene in the merits appeal.

The United States and AT&T now have agreed to settle the 1956 decree construction litigation by means of a Modification of the Final Judgment, a copy of which is attached. The agreed-upon Modification, which will be filed today in the district court in New Jersey, altogether removes the provisions of the 1956 decree at issue in these appeals. The Modification would terminate this litigation. It would also substantially alter the circumstances that underlie the suit that has been pending between the parties in the United States District Court for the District of Columbia and make further litigation in that action unnecessary. 2/ Accordingly, for the convenience of the parties and in the interest of efficient administration of justice, the parties are this day moving the district court for the District of New Jersey to transfer United States v. Western Electric Co. to the district court for the District of Columbia, so that this latter court will be able to rule on the parties' agreement to modify the Final Judgment.

Because the parties have agreed to modify the Final Judgment in a manner that eliminates the provisions in dispute on this appeal, there is no longer a live controversy before

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2/ United States v. AT&T, D.D.C., C.A. No. 74-1698.

this Court, and the merits appeal consequently is moot. See, e.g., J. Aron & Co., Inc. v. Mississippi Shipping Co., Inc., 361 U.S. 115 (1959); Steward v. Southern Ry. Co., 315 U.S. 784 (1942). See also Wilkinson v. Abrams, 627 F.2d 650, 657 (3d Cir. 1980); Dow Chemical Co. v. United States Environmental Protection Agency, 605 F.2d 673, 677-678 (3d Cir. 1979). Similarly, the intervention appeals are moot. Because there no longer exists any live controversy concerning the construction of the 1956 decree, there is no judicial proceeding in which to intervene.

When matters become moot during the pendency of an appeal, it is the duty of the appellate court to dismiss the appeals and to vacate the judgment below. See Great Western Sugar Co. v. Nelson, 442 U.S. 92, 93-94 (1979); United States v. Munsingwear, Inc., 340 U.S. 36, 39-41 (1950); Hart v. United Steelworkers of America, 482 F.2d 282, 283 (3d Cir. 1973). Consequently, the merits appeal and the intervention appeals should be dismissed, and the orders of the district court granting AT&T's motion for construction and denying the various motions to intervene should be vacated. This will ensure that there will be no prejudice to whatever rights the proposed intervenors

may have with respect to the joint motion to modify the decree.

Respectfully submitted.

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Counsel for Western Electric Company and American Telephone and Telegraph Company

CERTIFICATE OF SERVICE

I hereby certify that on this 8th day of January, 1982, I caused the foregoing Joint Motion of United States and AT&T to Dismiss Appeals on Grounds of Mootness to be served by hand delivery to the following:

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James H. Laskey

EXHIBIT 10

IN THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

UNITED STATES OF AMERICA, Plaintiff-Appellee, v. WESTERN ELECTRIC CO. and AMERICAN TELEPHONE AND TELEGRAPH CO., Defendants-Appellees; ALARM INDUSTRY TELECOMMUNICATIONS COMMITTEE, ET AL., Proposed Intervenors-Appellants.	Nos. 81-1960 and consolidated cases
UNITED STATES OF AMERICA, Plaintiff-Appellant, v. WESTERN ELECTRIC CO. and AMERICAN TELEPHONE AND TELEGRAPH CO., Defendants-Appellees.	No. 81-2837

JOINT MOTION FOR EXPEDITED CONSIDERATION
OF JOINT MOTION TO DISMISS APPEALS

The United States of America, Western Electric Co., and American Telephone and Telegraph Co. ("AT&T") hereby move for

expedited consideration of the joint motion to dismiss appeals filed herewith. As explained more fully in that motion, the parties are moving to dismiss these appeals as part of the settlement of this 1956 decree litigation. The settlement, in turn, will allow termination of another antitrust suit brought by the United States against AT&T in 1974, the trial of which is nearing completion in the United States District Court for the District of Columbia. The dismissal of these appeals will help assure prompt disposition of the motion in the district court below, joined by both parties, to transfer jurisdiction over the 1956 consent decree to the District of Columbia district court and the joint motion to modify the outstanding decree. Since the rights of all parties, proposed intervenors, and amici curiae would be protected fully in the anticipated decree modification proceedings in the District of Columbia, expedited consideration of the joint motion to dismiss the subject appeals would conserve both judicial and private resources without adversely affecting any litigant.

Respectfully submitted.

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Assistant Attorney General

RONALD G. CARR
Deputy Assistant Attorney General

BARRY GROSSMAN
JAMES H. LASKEY
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Counsel for Western Electric Company and American Telephone and Telegraph Company

CERTIFICATE OF SERVICE

I hereby certify that on this 8th day of January, 1982, I caused the foregoing Joint Motion for Expedited Consideration of Joint Motion to Dismiss Appeals to be served by hand delivery to the following:

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James H. Laskey

EXHIBIT 11

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, Plaintiff, v. AMERICAN TELEPHONE AND TELEGRAPH COMPANY, WESTERN ELECTRIC COMPANY, INC.; AND BELL TELEPHONE LABORATORIES, INC., Defendants.	Civil Action No. 74-1698

STIPULATION FOR VOLUNTARY DISMISSAL

Pursuant to Rule 41(a)(1)(ii) of the Federal Rules of Civil Procedure, the parties stipulate that the above entitled action is hereby dismissed without prejudice.

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For Defendants

William F. Baxter
Assistant Attorney General
Antitrust Division
Department of Justice
(202) 633-2401
For Plaintiff

Dated January 8, 1982

EXHIBIT 12

ORIGINAL FILED
JAN 11 1982
ANGELO W. LOCASCIO, CLERK

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY
Civil 17-49

January 11, 1982

UNITED STATES OF AMERICA, Plaintiff,

vs.

WESTERN ELECTRIC COMPANY, INCORPORATED, and AMERICAN TELEPHONE AND TELEGRAPH COMPANY, Defendants.

Appearances:

W. Hunt Dumont, Esq., U.S. Attorney, by Stephen Taylor, Esq., Asst. U.S. Attorney, (Newark), attorney of record; William F. Baxter, Esq., Assistant Attorney General Antitrust Division, by Ronald G. Carr, Esq., Deputy Assistant Attorney General (Washington, D.C.), of counsel, for plaintiff

Pitney, Hardin, Kipp & Szuch, Esqs., by S. Joseph Fortunato, Esq., (Newark), attorneys of record; Howard J. Trienens, Esq., George W. Cook, Esq., and Jim G. Kilpatric, Esq., (New York City), and Sidley & Austin, Esqs., by Robert D. McLean, Esq., (Washington, D.C.), of counsel, for defendants.

O P I N I O N

BIUNNO, District Judge.

On January 8, 1972, there were filed with the Clerk and submitted to the court in this case various papers designed to implement a disposition by settlement of the matters now pending before the United States District Court for the District of Columbia in the United States v. American Telephone and Telegraph Co., et al., No. 74-1698 (D.D.C.).

The papers submitted here disclose that as part of the disposition there was filed on December 8, 1981, in the District of Columbia, a voluntary dismissal of that pending action pursuant to Rule 41, F.R.Civ.P. upon stipulation of the parties under the provisions of (a)(1)(ii) of that Rule. There was also filed here a Modification of Final Judgment in this cause which, after the necessary recitals vacates in its entirety the final judgment entered by consent on January 24, 1956, and replaces it with the items and provisions agreed upon.

There was also filed, at the same time, a notice of motion returnable on February 8, 1972 or the earliest date established by the court, for an order to transfer this cause, Civ. 17-49, to the U.S. District Court for the District of Columbia, pursuant to 28 USC §1404(a), and a further motion for expedited consideration of the motion for transfer (i.e., as soon as feasible before the regularly noticed return date of February 8, 1982), and pertinent memoranda.

A reading of all of the papers now submitted, in the light of the pleadings herein, the final judgment of January 24, 1956, the proceedings in connection with defendants' motion to construe that judgment, and all other pertinent matters of record in this case, satisfy the court, after hearing the parties, that the Modification of Final Judgment stipulated to by the parties, should be entered at this time and without further delay.

Section XVII of the 1956 judgment expressly provided that jurisdiction be retained for a number of purposes including "the modification . . . of any of the provisions thereof."

The law seems to be entirely clear that, even without an express reservation of jurisdiction like the one here, it is a principle inherent in the jurisdiction of the chancery for a court of equity to be empowered to modify a judgment of perpetual duration to adapt it to current circumstances and conditions. See, for example, U.S. v. Swift & Co., 286 U.S. 106 (1932), for a case where the judgment to be modified was one entered by consent, and U.S. v. United Shoe Machinery Corp., 391 U.S. 244 (1968), for a case where the judgment to be modified was entered after trial and not by consent.

That there must be an adequate hearing to support modification is established by Hughes v. United States, 342 U.S. 353 (1952).

The hearing in this instance, aided by the informative record compiled on last year's motion to construe the 1956 judgment, satisfies the court that the stipulated Modification of Final Judgment negotiated by the parties should be entered. The reasons follow.

Since the complaint was filed here in 1949, about 4 years after the end of World War II, and since the final judgment of 1956 only 7 years later, there have been enormous and rapid changes both in technology and in regulatory methodology in the field of communications. A profile of the history was set out by way of context, of which the court took judicial notice, at the hearing held April 13, 1981. And, as observed there, every indication is that even more is yet to come.

Proceedings under the anti-trust laws brought by the United States present difficult and complex problems in any case. So long as the national economy is built upon the concepts of private enterprise and initiative, primarily financed by private capital formation and investment, it is inevitable that the articulation of detailed directions or restrictions in an anti-trust judgment (whether fashioned by a court after trial or by the parties through negotiation) carries with it a degree of risk that the concept of free enterprise and open competition will be degraded through some unsuitable confinement or invasion of sound business judgment.

It is true in principle that an enterprise may be so imaginative, creative, and diligent that by producing a superior product or service at the lowest feasible cost and with the highest achievable productivity, all of its competitors may abandon the field. This can occur without any kind of violation of any anti-trust law. Yet, it is a fact of life known to all who are familiar with the field that even such honestly earned success inevitably invites anti-trust charges. The consequence of this paradox is that otherwise sound business decisions are often withheld or restrained out of concern for the risk that antitrust suits may ensue, along with the massive expense and diversion of managerial talent that they always consume.

The problem is even more complex and difficult when the enterprise is a privately owned public utility subject to extensive, detailed and pervasive regulatory supervision at federal and state levels.

Subjection to pervasive state regulation does not, as a matter of law, furnish automatic insulation from federal anti-trust claims, as evidenced by Cantor v. Detroit Edison, 428 U.S. 579 (1976). The rationale of that case was simply that since the anti-trust laws are federal statutes, the authorization of challenged conduct under state regulatory law had to give way, in case of conflict, under the Supremacy Clause.

In cases, like this one, where pervasive regulation is by federal law, the Supremacy Clause has no application since anti-trust laws are statutes and not part of the Constitution. Thus in such cases the question becomes one of construing conflicts arising between different federal statutes. For some particular activities or conduct, the regulatory statute may expressly exclude application of the anti-trust laws. For others there may be nothing but silence on the point.

It is for this reason that anti-trust cases dealing with utilities extensively regulated by federal agencies are especially difficult in terms of the risk that the terms of a judgment may interfere more or less with the effective functioning of the regulatory agency.

The extensive history of the litigation involving the merger of the Pennsylvania Railroad and the New York Central Railroad is probably a classic example. During the lengthy process before final approval the terms and provisions initially agreed on had been so greatly altered, and the economic and operating conditions had so changed, that both parties may have been better off had they cancelled the merger proposal. No one will ever know, of course, but it is not unlikely that imposed conditions to include other railroads that were on the brink of failure, among other things, helped to load to the eventual demise of the merged railroads.

In brief, litigated anti-trust cases of any magnitude are inherently inefficient instruments for achieving the statutory policy, consuming as they do tremendous amounts of professional time and expense, as well as managerial talent, not to mention the heavy burden on the courts. When they are tried to a jury, they are even more consuming of time and expense, and carry the extra risk that some error in the instructions to the jury in such complex matters may well lead to a repetition of the process through reversal with direction for a new trial.

The usual long duration of such cases carries another concealed cost which can be quite high, namely the cost to the enterprise involved from the withholding of ordinary business decisions while the litigation proceeds and until the outcome is known.

A further cost, also a concealed one, is in the cost of supporting inefficient producers as the consequence of the provisions of an anti-trust judgment. That cost is inevitably reflected in higher prices to the general public in the aggregate for the product or service involved.

At the 1957 Annual Meeting of the American Bar Association in London, the late Thurman Arnold, Esq., then Assistant Attorney General in charge of the Anti-Trust Division, delivered a paper outlining the policy followed under his administration. Instead of merely filing anti-trust suits and litigating them, his office conducted the necessary investigation and prepared a draft complaint. The potential parties were then invited to inspect the complaint and engage in negotiations. The usual outcome was a revised complaint, an answer and a consent judgment, all three of which were filed and entered on the same day. This technique provided means for participation and consultation with other agencies, some regulatory and others users of the product or service, and made trial unnecessary.

Mr. Arnold did not invent this method, of course. It was used at least as far back as 1920, as mentioned in Judge McLaughlin's opinion in U.S. v. Swift & Company, 158 F.Supp. 551, at 553 (D.D.C.,1958).

The new anti-trust case in the District of Columbia has been pending there since November 20, 1974, more than 7 years ago. A lengthy trial of the issues has been only partly completed. It includes the issue whether any of the claims made there are barred by res judicata arising from the 1956 judgment here. No matter what the eventual outcome, at least one appeal would have been inevitable, with a massive record to boot.

To the extent that any claim might have been held barred by the 1956 judgment here, that result would not have ended the matter, since the United States could have applied here for additional restrictions on one or another kind of activity by way of modification.

All of these uncertainties are brought to an end by the agreement to dismiss the 1974 suit without prejudice, to enter the Modification of Final Judgment here, and by the motion to transfer the case to the District of Columbia.

It is accordingly plain, from the structure of the modification that the disposition arrived at could not have been achieved without substituting the new provisions for those of the 1956 final judgment.

Its terms call for divestiture, by spin-off of stock or other disposition, of the operating companies, referred to as BOC's, of which there are 22. Not only will this major change bring about the existence of 22 independent operating companies which may be organized into one or more groups, but it holds hope of eliminating, or at least reducing, the present separations system now required under 57 C.F.R. §67.1 (1969), at least for division of revenues and no doubt for other purposes as well. That system, unavoidably needed now, is extremely complex and probably understood only by a specialized few. Eliminating or reducing it will greatly lessen the tasks of federal and state regulatory agencies as well as the expense it places on the utility, which in the end must be paid for by the customer. In this regard, unlike most anti-trust judgments, an overhead regulatory expense will be reduced or eliminated and the public will receive the benefit.

The structure of the negotiated arrangements carries other benefits in the public interest. It will advance the FCC policy to open up competition for customer provided equipment, developed since the Carterfone decision as well as for interexchange services since the MCI decision. It should also aid in bringing to reality the advantages to the national communications network labored to be achieved by the FCC decisions after its computer inquiries, and hopefully may render moot the appeal therefrom now pending in the Court of Appeals for the District of Columbia. If it does not render it moot, it may provide a basis on which the FCC can modify its orders in ways that will protect them from any serious or substantial challenge.

The concept of cutting the operating companies loose as independent enterprises is not new. It has occurred for a long time to many perceptive observers as a method for constructively eliminating a vast amount of endless controversy over intractable issues. These observers were mostly involved in the regulatory process which has become incredibly complex, difficult and expensive.

That the defendants have conceived this course carries no implication whatever that the anti-trust laws have ever been violated by them in any way. The 1956 final judgment carried no such implication, and the present Modification of it carries none.

Rather, as the court regards the matter, it reflects a careful business decision which effectively evaporates any subjective perception of anti-trust violation while preserving the integrity of the national communications network and the economic and operating viability of the BOCs, as well as of competitors. It is clearly not designed to provide wasteful support for inefficient producers. It removes bonds which have undoubtedly restrained domestic enterprises and frees them to meet on the merits of the marketplace the inevitable future competition from others, in parts of the world where there are not any anti-trust laws and where efficient cartels, with governmental support, are encouraged. The new structure will test the issue whether free enterprise can meet the challenge of that kind of competition.

The only aspect mentioned anywhere that suggests a public disadvantage is the view that one consequence of the change may be that the cost, and therefore the charges, for local calls will rise more sharply than those for interstate calls. This view is based on the proposition that at present, revenues of the parent from interstate service helps absorb costs of intrastate service, and that business customers make much more use of interstate services and so will reap this benefit.

As the court sees it, this view is faulty on two or three grounds. If it be true that interstate revenues have been supporting local costs, then the regulatory process has been faulty. Neither class of service, in principle, should be called upon to support the other.

Second, as is known to all familiar with the subject, business communications charges tend to run about double those for residential service. This is due to the obvious fact that business use is high and concentrated within the usual business hours. Individuals are either at home or at work at any given moment. While they are at work they can only use business phones (even if they use them for personal calls) and physically cannot use their residence phone which is at home. This business peak, like similar peak demands on other kinds of public utilities, obliges the utility to obtain and operate the plant, equipment and personnel to satisfy the demands of the peak, and the business user is rationally charged for this incremental added cost. In the long run, of course, this differential washes out because the expense of business calls is a business expense for income tax purposes, so the out-of-pocket cost to a business user ends up at roughly the same amount as the non-deductible phone costs of the residential user.

Third, if it be true that interstate revenues have been supporting local costs, modern technology and regulatory policies provide means to the large interstate business user to avoid or escape any contribution to that economic support. Such users are free to establish their own networks, via microwave relay or communication satellites, on their own or through private contract carriers. An interstate transmission by satellite involves no more cost between New York and Trenton than it does from New York to San Francisco. The reason is that the distance up to the satellite and back, a combined distance of some 45,200 miles, is hardly affected by the base of the triangle. Satellite communication is headed for growth, not decline, and so if large users of the interstate wire network feel they are being overcharged to support local calls, they will soon enough find ways to reduce their costs. This is the essence of competition.

The format of the Modification reflects a carefully considered and undoubtedly wise business decision on the part of the parent company to emancipate each and all of the 22 operating companies formally, officially and in a complete legal sense. As a pretrial matter, the operating companies have long since been emancipated, with their business conducted in much the same fashion as divisions of a single corporation are when managed on a decentralized basis.

The decentralized, divisional system of operation of large enterprises has been recognized for some decades as a business administrative structure that furnishes strong local responsibility and initiative or motivation. At the same time, sophisticated comparative analyses of divisional activity have long provided not only a reliable management tool for the measurement of the effectiveness of operations and the financial efficiency and productivity of each unit, but it has also provided a form of intracorporate competition to stimulate officers and employees at all levels of each unit to perform to the best of their ability in order to compete with the other units. As a matter of practical fact, then, the change will give legal format to the internal mode, and the court sees no disservice to the public interest in the process.

At the same time, the fragmentation of the manufacturing arm, which could have achieved nothing but inefficiency and waste, with consequent increased cost to the public, is avoided. Also, the research arm, represented by the Laboratories, is enabled to continue, as it could not have otherwise. In many ways, the Laboratories are a modern equivalent of the incredibly stimulating Academy sponsored by Lorenzo the Magnificent in the brightest days of the Renaissance, in an institutional sense. Only the team gathered at Jena in the 1800's to develop optical glasses and lenses, and the pioneering chemists assembled to open the doors to polymer chemistry in the early part of this century, have even approached it. Perhaps the genius and perspiration of Thomas A. Edison and his devoted staff, should be included.

For each and all of the foregoing reasons, the court concludes that the stipulated Modification is fully supported by the dramatically changed circumstances, that it is consistent with the pleadings and the objects of the suit in this district, and is in the general public interest. The order has accordingly been signed.

The motion for transfer will be decided separately on another date, and as early as feasible. The court's research on this motion has not been completed. The separate disposition of the motions carries no implication of any doubt of the propriety of the transfer. It appears to be authorized by law. The court merely wishes to assure itself that all potential procedural aspects have been dealt with correctly. It would be imprudent to act quickly for the sake of expedition only to find an unexpected problem that might have been resolved and avoided.

In any event, as the court understands it, the main object of the transfer is to provide means for close supervision of the phased stages in this complex change of corporate structure in the District of Columbia where Judge Greene's intimate familiarity with the details of the trial up to this point will better equip him to deal with the transition.

The parties may wish to inform the Court of Appeals in this circuit of this opinion and of the entry and filing of the Modification, as this may be pertinent to the motions now pending there.

s/ Vincent P. Biunno, U.S.D.J.

Original to Clerk
xc: All counsel

EXHIBIT 13

JAN 19 1982

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY
Civ. 17-49

UNITED STATES OF AMERICA, Plaintiff,

vs.

WESTERN ELECTRIC COMPANY, INCORPORATED
and AMERICAN TELEPHONE AND TELEGRAPH COMPANY, Defendant.

CORRECTED ORDER

For the reasons articulated in a supplemental opinion to be filed as soon as feasible,

It is, on this 14th day of January, 1982, ORDERED that the motion of the United States, filed in this cause on January 8, 1982, to the extent decision thereon was reserved, is hereby disposed of as follows:

1. All issues, matters and proceedings arising out of orders of this court in disposing of the post-judgment proceedings begun by the filing of defendants' motion for construction of the final judgment of January 24, 1956, which motion was filed March 4, 1981, and which are the subject of appeal and other proceedings before the Court of Appeals for the Third Circuit, are hereby severed from this case.

2. Except for the portion so severed, this case is hereby transferred to the United States District Court for the District of Columbia.

3. All papers now in the physical possession of the Clerk of this Court, that have been or are hereafter filed, on or after January 8, 1982 shall be forwarded by said Clerk to the Clerk of the United States District Court for the District of Columbia, retaining, however, in the files of this court, true copies of all such papers including the docket entries thereof.

4. The parties shall promptly furnish to the Clerk of the United States District Court for the District of Columbia true copies of the complaint herein, the answer of both defendants, the Final Judgment signed and filed January 24, 1956 and of such other papers as may be directed to be filed there by that court.

5. Jurisdiction is reserved to correct typographical errors in the transcript of the hearing of April 13, 1981, filed April 22, 1981, as well as of the hearing of January 11, 1982, filed January 11, 1982, and such corrections shall be forwarded by the Clerk of this Court in accordance with paragraph 3, above.

6. Jurisdiction is further reserved to enter a further order of transfer to said United States District Court for the District of Columbia so much of the issues and matters and proceedings as are severed by paragraph 1, above, after the filing in this court of the mandate, or order in lieu of mandate, of the United States Court of Appeals for the Third Circuit, and in compliance with the directions thereof including the entry of any orders so directed.

January 14, 1982

s/ Vincent P. Biunno, U.S.D.J.

Original to Clerk
xc: All counsel
Hon. Harold H. Greene

U.S. Department of Justice

Antitrust Division

EXHIBIT 14

Office of the Assistant Attorney General *Washington, D.C. 20530*

JAN 18 1982

Honorable Harold H. Greene
United States District Court
for the District of Columbia
Washington, D.C. 20001

Dear Judge Greene:

On January 12, 1982, the Court indicated its concern with the procedural posture of the proposed modification of the Consent Decree entered in 1956 in United States v. Western Electric Company, Inc. and American Telephone and Telegraph Company, 1/ and in particular with any possibility that the procedures of the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16(b) et seq. ("Tunney Act"), might not be followed in connection with the entry of the modified Decree. The Court asked the parties to advise it not later than January 18 whether the proposed modification will be submitted to it for application of those procedures.

It is and always has been the intention of the parties to follow the procedures of the Tunney Act in connection with the entry of the modified Decree. 2/ It is and always has been our intention to follow those procedures in this Court. Because the modified Decree will require a basic restructuring of the telecommunications industry, it necessarily affects vital public concerns. In these circumstances, it is altogether appropriate that there be a complete exposition of the Decree's merits before this Court, which, as a result of the trial of

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1/ 1956 Trade Cas. ¶ 68,246 (D.N.J. 1956).

2/ The United States believes that the Tunney Act does not by its terms apply to modifications of existing decrees, most of which involve slight adjustments of concern only to the immediate parties. With respect, however, to major decree modifications, the Tunney Act's procedures and standards help facilitate thorough exposition and review. Accordingly, the United States has followed comparable procedures in connection with major decree modifications. See United States v. General Electric Co., Civil Action No. 28228 (E.D. Pa.), judgment modified September 19, 1977,

United States v. AT&T, has substantial expertise on the competitive situation in the telecommunications industry, and the likely effects on that industry of the restructuring the modified Decree requires.

In recognition of the need for thorough exposition of the modified Decree before this Court, and for a determination by this Court that the Decree is consistent with the public interest, the parties moved for transfer of this cause from the United States District Court for the District of New Jersey to this Court immediately upon filing the proposed modified Decree, and requested expedited consideration of the transfer motion. 3/ Copies of these moving papers and accompanying memoranda have been provided to this Court. The New Jersey District Court, by the attached order, granted the transfer motion on January 14, 1982. The parties are undertaking immediately all steps necessary on their part to comply with the transfer order. Once the mechanics of transfer are completed, the United States and AT&T will take all steps prescribed by the Tunney Act to assist this Court's public interest determination. 4/ In particular, the

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2/ (CONTD) 1977-2 Trade Cas. ¶ 61,660, proposed modification, memorandum in the nature of a competitive impact statement, comments, and responses published in 42 Fed. Reg. 17004; United States v. Swift & Co., Civil Action No. 58 C 613 (N.D. Ill.), judgment modified January 25, 1980, 1980-1 Trade Cas. ¶ 63,185, summary of proposed modification and notice of hearing published in 44 Fed. Reg. 63160.

3/ The parties also moved to dismiss as moot the Government's appeal of a recent construction of the 1956 Decree by the District Court in New Jersey, and to dismiss appeals by would-be intervenors in that case, in order to facilitate the transfer. United States v. Western Electric Co. and American Telephone and Telegraph Co., No. 81-2837 (3d Cir.) (motion to dismiss filed January 8, 1982); United States v. Western Electric Co. and American Telephone and Telegraph Co., Alarm Industry Telecommunications Committee, et al., Proposed Intervenors-Appellants, Nos. 81-1960 and consolidated cases (3d Cir.) (motion to dismiss filed January 8, 1982).

The interests of the would-be intervenors, and others, in the terms of the modified Decree can be completely protected by this Court during its consideration of the Decree's merits.

4/ That the modified Decree has, technically, been approved and entered by the Court in New Jersey in no way alters this intention. Upon transfer, this Court will acquire and retain jurisdiction over the Decree, including the power to consider the effects of the Decree on the public interest, see generally, United States v. Swift & Co., 1975-1 Trade Cas. ¶ 60,201 (N.D.

United States will meet the Act's publication requirements as soon as possible.

In short, the New Jersey District Court's transfer order assures that the merits of the modified Decree can be fully aired before this Court. This is precisely what the parties have intended all along.

Sincerely,

William F. Baxter
Assistant Attorney General
Antitrust Division

cc: George L. Saunders, Esq.

4/ (CONTD) Ill. 1975); see also, United States v. General Electric Co., 1977-2 Trade Cas. ¶ 61,659 (E.D. Pa. 1977) and United States v. American Cyanamid Co., 1974-1 Trade Cas. ¶ 74,950 (S.D.N.Y. 1974).

EXHIBIT 15

AT&T

American Telephone and
Telegraph Company
499 South Capitol St., S.W.
Washington, D.C. 20003
Phone (202) 488-6500

January 18, 1982

Honorable Harold H. Greene
United States District Court
for the District of Columbia
Washington, D.C. 20001

Dear Judge Greene:

Pursuant to the Court's request of January 12, 1982, the Department of Justice is reporting by separate letter on the parties' successful efforts to transfer United States v. Western Electric Company, Inc. and American Telephone & Telegraph Company, Civil Action No. 17-49, from the United States District Court for the District of New Jersey to the United States District Court for the District of Columbia for proceedings in keeping with the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16(b) et seq. ("Tunney Act").

By this letter, defendants join in plaintiff's report.

Very truly yours,

Jim G. Kilpatric
General Attorney

cc: Gerald Connell, Esq.

EXHIBIT 16

ORIGINAL FILED
JAN 20 1982
ANGELO W. LOCASCIO, CLERK

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY
Civ. 17-49

January 20, 1982

UNITED STATES OF AMERICA, Plaintiff,

vs.

WESTERN ELECTRIC COMPANY, INCORPORATED, and AMERICAN TELEPHONE AND TELEGRAPH COMPANY Defendants.

Appearances:

W. Hunt Dumont, Esq., U.S. Attorney, by Stephen Taylor, Esq., Asst. U.S. Attorney, (Newark), attorney of record; William F. Baxter, Esq., Assistant Attorney General Antitrust Division, by Ronald G. Carr, Esq., Deputy Assistant Attorney General (Washington, D.C.), of counsel, for plaintiff

Pitney, Hardin, Kipp & Szuch, Esqs., by S. Joseph Fortunato, Esq., (Newark), attorneys of record; Howard J. Trienens, Esq., George W. Cook, Esq., and Jim G. Kilpatric, Esq., (New York City), and Sidley & Austin, Esqs., by Robert D. McLean, Esq., (Washington, D.C.), of counsel, for defendants.

SUPPLEMENTAL OPINION

BIUNNO, District Judge

This opinion supplements that of January 11, 1982 and rules on the transfer motion then reserved. An order to sever and transfer was signed January 14, 1982, the reasons for which are articulated here. 1/

Transfer under 28 USC §1404(a).

Before the effective date of the 1948 Judicial Code, Pub. L. 80-773, Act of June 25, 1948, §38, effective September 1, 1948 the federal courts lacked statutory authority to transfer a case from one district to another just as, even today, a case pending in the courts of one State cannot be transferred to the courts of another State, and a case pending in a State court generally cannot be transferred to a federal court or vice-versa, although other mechanisms are available for similar purposes in special instances. See, for example, 28 USC §1441 through §1451, dealing with the removal of certain civil actions or criminal proceedings from a State court to a federal court, including remand of the case to the State court from which it was removed, 28 USC §1447(c). Also, where suit is begun in a federal court, abstention under the doctrines of Railroad Comission of Texas v. Pullman Co., 312 U.S. 496 (1941) and Younger v. Harris, 401 U.S. 37 (1971) may have some of the practical effects of transfer of the dispute (though not of the action) to a State court.

The interplay between the lack of authority to transfer cases between federal courts, and the statutes regulating venue, is highlighted by the decisions involving the Federal Employers' Liability Act, venue for which is provided in 45 USC §56, and the antitrust laws, venue for which is provided in 15 USC §22.

Before the 1948 Judicial Code, it was held that actions of this kind were not open to objection on the doctrine of forum non conveniens, Baltimore & Ohio R. Co. v. Kepner, 314 U.S. 44 (1941) (FELA case); U.S. v. National City Lines, 334 U.S. 573 (1948) (anti-trust case).

The National City case was decided June 7, 1948, before enactment of the 1948 Judicial Code. The district court, presented with a motion raising forum non conveniens, and lacking authority to transfer, dismissed the case on that ground, 7 FRD 456 (D. Cal., 1947). The Supreme Court reversed, ruling that the doctrine did not apply to anti-trust suits as it had earlier ruled it did not apply to FELA suits.

After the effective date of the 1948 Code, the motion was renewed and again granted, this time by an order to transfer the case to Chicago, 80 F. Supp. 734 (D.Cal.,1948). See, also, U.S. v. E.I. Dupont, etc., 83 F. Supp. 233 (D. Colo. 1949).

The second order came before the Supreme Court indirectly, through a motion by the United States for leave to file a petition for certiorari, and hearing was set on that motion, 335 U.S. 897 (1948).

The motion was ruled upon on the same day that the Supreme Court decided Ex parte Collett, 337 U.S. 55 (1949) and Kilpatrick v. Texas etc., Co., 337 U.S. 75 (1949), both being FELA cases. In the Collett and Kilpatrick cases, the court concluded that with the availability of authority to transfer cases by change of venue under 28 USC §1404(a), the reason for denying the doctrine of forum non conveniens had been eliminated, and hence the doctrine was available in FELA cases.

This view was adhered to in the disposition of the second U.S. v. National City Lines case, 337 U.S. 78 (1949) and applied to anti-trust cases as well by denying leave to file a petition for certiorari.

The rationale rested mainly on the Congressional history reflecting the revisor's notes prepared by Professor Moore, and discussed in some detail in Moore, "Federal Practice", ¶ 0.145 [4.-1].

With this trilogy, any doubt that §1404(a) was available in both FELA and anti-trust cases was erased.

Limitations on transfer.

There are now two general statutes authorizing transfer by change of venue, 28 USC §1404 and §1406. The first applies when the venue of a pending case is correct, but considerations of convenience of parties and witnesses, in the interest of justice, warrant a transfer.

The second applies when venue of the filed case is in the wrong district or division. In this instance, dismissal is specified unless the interest of justice warrants transfer instead (as, where the statute of limitations may have since run out).

So long as the transferor court had subject-matter jurisdiction of the case, a transfer is permitted even though in personam jurisdiction over the party may have been lacking, see Goldlawr v. Heiman, 369 U.S. 463 (1962), and U.S. v. Berkowitz, 328 F.2d 358 (CA 3, 1964).

Under both sections, however, it is essential that the transferee court be one in which the action "might have been brought". From the standpoint of venue, this limitation is controlled by the particular statute governing venue and the circumstances in respect to venue when the complaint was filed. See, e.g., Fourco Glass v. Transmirra, 353 U.S. 222 (1957); Hoffman v. Blaski, 363 U.S. 335 (1960). In Corporate etc. v. Dubner, ___ F. Supp. ___ (D.N.J. Civ. 81-1608, 1/11/82), this court declined to follow Welch Scientific Co.

v. Human etc. 416 F.2d 32 (CA 7, 1969), cert. den. 302 U.S. 1003 (1970) in a patent case and denied transfer because venue here was clearly proper and a transfer was of doubtful authority. This was because of the special venue requirements of 28 USC §1400(b).

In this case, there is no such doubt. The applicable venue statute is 15 USC §22, which allows venue to be in a district (a) where the defendant is an inhabitant; (b) where a defendant may be "found", or (c) where a defendant transacts business. See Sunbury etc., v. U.S. Steel, 230 F.2d 511 (CA 3, 1956). It is clear from the pleadings and the 1956 final judgment here that both defendants are doing business in the District of Columbia, and were doing business there when the complaint in this case was filed. That district, then, is one where the 1949 action "might have been brought", and so is a district to which there is statutory authority to transfer the case.

It should be observed, too, that 15 USC §22 not only sets the criteria for venue, but also authorizes process to be served in any district of which the defendant is an inhabitant or where it may be found. This is similar to the authorization in 28 USC §2361 for actions of interpleader or in the nature of interpleader, and makes it unnecessary to consider whether either or both defendants could be served with process effectively out of the District of Columbia under its "local law."

Multidistrict litigation.

The court has also examined the statute on multidistrict litigation, Pub. L. 90-296, 82 Stat. 109, April 29, 1968, as amended, 28 USC §1407. There are two reasons it does not apply. One is that §1407 is intended by its tenor to apply to "pending" cases, i.e., cases that have not yet gone to judgment, and its main object is to coordinate or consolidate for pretrial proceedings. The suit here went to final judgment on January 24, 1956, and in a closed case with reserved jurisdiction for a wide variety of post-judgment proceedings to carry out a number of continuing provisions, or to construe it, or modify it, or enforce it as it stood, or as construed or modified. Similarly, the new 1974 anti-trust case filed in the District of Columbia was well into the trial stage when the various papers were filed and could hardly be said to involve pretrial proceedings.

The second reason is that §1407 (g) makes the statute inapplicable to any action in which the United States is a complainant [sic] arising under the anti-trust laws. 2/

Factors supporting transfer.

As the record of the hearing of January 11, 1982 shows, the papers submitted to this court on January 8, 1982 and on January 11, 1982 indicated that the parties had filed a stipulation of dismissal of the 1974 action in the District of Columbia under F.R.Civ.P.41(a)(1)(ii); a joint motion in the U.S. Court of Appeals for the Third Circuit to dismiss as moot Case No. 81-2837 (that being the appeal by the United States from this court's 1981 order construing the final judgment) and a number of other cases related to it on behalf of applicants who had been denied intervention here although all were permitted to make submissions amicus curiae: and a joint motion in the Court of Appeals for expedited consideration of the dismissal requested. These were aside from the papers filed here.

The papers filed with the Court of Appeals, copy of which was handed up at the January 11th hearing (see Tr.,p.15, lines 11 to 22), state that the parties had resolved the litigated dispute before it over the construction of the 1956 final judgment by means of the Modification of Final Judgment. The Court of Appeals was told that the agreed-upon Modification filed that day in this court, removed the matters at issue on the appeal and so terminated that litigation. It was told that it would substantially alter the circumstances underlying the 1974 suit (D.DC, Civ. No. 74-1698)

and make further litigation there unnecessary. It was also told of the motion here to transfer this 1949 case to the District of Columbia.

The papers filed here made it clear that the parties desired a transfer of the entire 1949 case to the District of Columbia for the convenience of the parties and witnesses and in the interests of justice, under 28 USC §1404(a), so that proceedings relating to the modification of the 1956 final judgment here could be conducted in the District of Columbia court.

This view was confirmed at the hearing of January 11, 1982, where both sides agreed that there were two aspects before the court: the modification on stipulation and the transfer (Tr. p.3, lines 13-16; p. 16, lines 1-9).

The modification itself, which the court had studied along with the other papers on January 8, 9 and 10, outlined a pattern calling for the parent company to dispose of its interest in the 22 operating companies (BOCs) by means of a spin-off of stock or other disposition, along with other structural and organizational changes. In sum, a series of steps or stages was contemplated, starting with submission of a plan of reorganization within 6 months, to be completed within 18 months.

Submission of the plan, and specified steps for implementation, is to be submitted to the Department of Justice for its approval. Even after the reorganization is completed, each BOC is to submit (within 6 months thereafter) to the Department of Justice procedures to ensure compliance with specified requirements. There are also visitorial provisions, and in Appendix B there are structural and operational details for the BOCs, with specific deadlines on a variety of complex aspects including methods for eliminating the division of revenues process where interexchange plant, equipment and services are involved.

In sum, the Modification of Final Judgment sets lines of direction, with boundaries and timetables, which will involve efforts and steps for completion running, in at least one instance, to September 1, 1986. No doubt the parties will be able to attend to the details in most instances, but there are bound to be others where the court's assistance will be helpful.

It is this aspect which largely supports the motion for transfer, as noted by the United States at the hearing of January 11, 1982 (Tr. p. 16, line 10 to p. 17, line 14). There are the factors of potential need for day-to-day appearances, as well as access to an available court to resolve problems of phrasing and the like, for which jurisdiction is reserved under the modified final judgment.

Both sides agreed that the business decision to turn the BOCs loose effectively eliminates the basic ground for controversy underlying the case, and is one that was available to make without regard to the existence of any antitrust suit. (Tr., p. 17, line 17 to p. 18, line 10).

Inspection of the original pleadings here shows, contrary to some popular misconceptions, that the 1949 suit was by no means confined to seeking divestiture of the manufacturing arm (and the complaint asked that it, too, be dismembered), but also sought divestiture of the BOCs. While the case was settled along other lines in 1956, the modification submitted is well within the scope of the original complaint.

The exposure of Judge Harold H. Greene to the day-to-day detail presented during the months of trial in the separate District of Columbia case was seen as a means to equip him to deal with the numerous details with great facility as the framework set by the modification was executed (Tr. p. 16, line 16, to p. 17, line 16). This factor, added to the preference of the parties, weighs heavily in favor of the requested transfer as satisfying the interests of justice as well as the elements of convenience specified by 28 USC §1404(a).

For all these reasons, the court was completely satisfied that in the exercise of sound discretion, the motion for transfer should be granted. There were only procedural details to be looked into, and the decision to transfer was reserved only to allow time for their study and resolution.

Procedural aspects.

The order presently on appeal to the United States Court of Appeals for the Third Circuit in connection with the 1981 motion to construe the 1956 final judgment was no doubt appealable at least under the collateral order doctrine articulated in Cohen v. Beneficial Industrial Loan Corp., 337 U.S. 541 (1949) and other cases in the line.

As noted above, the 1956 final judgment contained many provisions operative in perpetuity so long as that judgment stood. The Appendix to this opinion classifies, in very condensed fashion, the variety of matters brought before the court in this fashion on a post-judgment basis. The 1956 final judgment itself was not appealable because its entry was by consent. The several appeals on post-judgment motions, to both the Supreme Court and the Court of Appeals, did not suspend the trial court's jurisdiction to continue to deal with other post-judgment matters as they arose. None of these was an appeal from the final judgment itself.

Thus, the pendency of the present appeal from the 1981 orders on the defendants' motion to construe in no way prevented this court from taking up and deciding other post-judgment motions, any more than an appeal from an interlocutory order granting or denying a preliminary injunction, allowed under 28 USC §1292(a)(1), does not take the entire case away from the trial court, which may proceed with pretrial aspects, trial and final judgment itself even while the interlocutory appeal is pending. The difference is one only of time: the usual interlocutory appeal is before final judgment, while all the proceedings here since January 24, 1956 have been post-judgment matters.

This, it seemed to the court, made it essential that the question of entering and filing the stipulated Modification of Final Judgment here had to precede the matter of transfer. Absent such entry and filing, it appeared that the achievement of mootness which was the basis of the motion for dismissal of the present appeals by vacating the challenged order could be no more than promissory or anticipated rather than mootness in fact.

Even with the modification signed and entered, procedural obstacles stood in the way of entering an order for transfer. The appeal then pending had caused the physical possession of the entire case file to be delivered to the Clerk of the Court of Appeals in Philadelphia. This was noted at the hearing, Tr. p. 14, line 22 to p. 15, line 10. As of late afternoon on Thursday, January 14, 1982, the information available from the Clerk's office in Philadelphia was that the motion to vacate and dismiss as moot, and the motion to expedite that motion, had not yet been assigned to a panel of the court and that January 18th had been set as the deadline for submitting any papers on the motions.

Recognizing that the equity and debt securities of defendants, and of the BOCs, are very widely held and that uninformed and misleading accounts of the technical legal aspects could render considerable disservice to investors having no part in the case but exposed to various risks by it, the court concluded that the general public interest as well as the need for stability in the securities markets called for rapidly designing a sound basis for entering an order for transfer as soon as possible.

The only secure and sound procedure for this purpose turned out to be to sever that part of the case now pending before the Court of Appeals and order the rest transferred

now, with jurisdiction reserved to transfer the severed segment, after the docketing here of the mandate, or order in lieu of mandate, of the Court of Appeals. It is on this design that the order of January 14, 1982 was drafted and signed.

Other procedural points present no difficulty. That a plaintiff may apply for transfer is widely accepted. See the decisions cited in Wright, Miller & Cooper, "Civil", §3844, footnote 5, and the few cases contra are not persuasive or involved other circumstances. Also, it is clear that transfer is authorized at any stage, even long after a final judgment, for which the prime instance is U.S. v. Swift & Co., 158 F. Supp. 541 (D.DC, 1958), transferring an anti-trust case 38 years after final judgment.

There is no attempt here to transfer this case to another district and to order it consolidated with another case already pending there, this being a step the court could not take, see Swindell-Dressler Corp. v. Dumbauld, 308 F.2d 267 (CA 3, 1962).

Rather, the procedure selected to expedite the transfer is one involving the combined use of F.R.Civ.P. 42(b) to sever so much of the case as is before the Court of Appeals, and 28 USC §1404 (a) to order transfer now of the remainder. There is precedent for this mode for achieving the objectives of F.R.Civ.P. 1: see Leesona Corp. v. Cotwool Mfg. Corp., 204 F. Supp. 139 (D.S.C., 1962), appeal dismissed 308 F.2d 895 (CA 4, 1962); Harvey Hubbell, Inc. v. The Rucker Co., 174 USPQ 17 (D-Ill., 1972). The decision in Alabama v. Blue Bird, etc., Co., 573 F.2d 309 (CA 5, 1978) is not regarded as a holding to the contrary, as the circumstances of that case were quite unique involving as they did what might be called a "star shell" of multiple severances and transfers to a large number of districts. No adverse factor resembling that is present here.

The 1974 Statute.

Consideration was given to the question whether Pub. L. 93-528, 88 Stat. 1706, 15 USC §16 (b) through (h), as added in 1974, had any application here. The point had been noted earlier in another context in the Memorandum Order dated April 15, 1981. The statute is clearly prospective, and this case had been disposed of by final judgment entered nearly 19 years before. Congress could hardly have intended that every final judgment theretofore entered since the enactment of the anti-trust laws should fall within the scope of the Act because of the entry of an order of construction or modification for which jurisdiction had been reserved.

The 1976 amendment to subsection (i), Pub. L. 94-435, is not relevant, nor is the 1980 amendment, Pub. L. 96-349, especially since by §5(h) of that act it was expressly made inapplicable to actions brought before its effective date of September 12, 1980.

In any event, the parties have indicated in their filed papers and in statements on the record in both courts, their intention to carry out steps paralleling those set out in the Act.

If any adjustment in time schedules should be called for on that account, or for any other reason, the Modification itself carries ample authority in the court to make such changes as may be needed, and this appears to be the understanding of the parties, see Tr. p. 17, lines 3 to 16.

s/ Vincent P. Biunno, USDJ

Original to Clerk
xc: All counsel

APPENDIX.

Between the date the complaint was filed on January 14, 1949 and the date the final judgment by consent was filed on January 24, 1956, the only formal activity in the case consisted of the issuance of summons and the making of returns, notice of allocation and assignment, stipulations and orders extending the time for answer, the filing of answer, and a number of motions in respect to discovery, orders thereon, and the like.

After the entry of the judgment, aside from a statement of taxed costs and a warrant for their satisfaction, the docket sheet discloses a variety of matters acted on over the years. For convenience, these are classified as follows:

...4 orders approving purchasers under Section IV (C) of the final judgment;

...27 undertakings by various persons pursuant to Section X of the final judgment;

...11 releases to various persons as identified and specified in each;

...proceedings on a motion by an applicant for patent license for relief from Section X of the final judgment;

...proceedings on motion of a person for leave to intervene as a party plaintiff in order to enforce compliance with and to punish for alleged violation of, the final judgment (including appeal to and affirmance by the Supreme Court of the United States);

...proceedings on a motion of an applicant for patent license to determine reasonable royalties under Section X(b) of the final judgment (including appeal to and affirmance by the United States Court of Appeals for the Third Circuit);

...proceedings on a motion by another applicant for patent license to determine reasonable royalties under Section X(b) of the final judgment (including extensive proceedings in aid of discovery for use in separate civil litigation in the U.S. District Court for the Southern District of Florida), concluded by withdrawal;

...proceedings on a motion by defendants for a construction of the final judgment (under Section XVII thereof); the motion was filed March 4, 1981, followed by more than a dozen motions and applications for intervention or to participate amicus curiae, or for other purposes. Hearing was held April 13, 1981 and all applicants were allowed to submit papers amicus curiae including factual summaries as context. Intervention as parties was denied, and the applicants filed more than eight provisional or protective notices of appeal. The opinion on the merits was filed September 4, 1981, and the order thereon was filed September 23, 1981. Notice of appeal from that order was filed by the United States on October 30, 1981 and was followed by further protective notices of appeal by applicants for intervention. This segment of the case is pending in the United States Court of Appeals, and is the

segment severed by the order of January 14, 1982. A certified copy of an order of the Court of Appeals, filed in this court on January 4, 1982, indicates that the United States had been granted an extension of time to file briefs.

...proceedings on a motion to transfer the case to the U.S. District Court for the District of Columbia, with executed stipulation and consent of the parties for modification of the final judgment, and order for Modification of Final Judgment, briefs and memoranda, all captioned in the cause in this court. Hearing was had January 11, 1982, and opinion granting modification along with order for Modification of Final Judgment was filed January 11, 1982, with reservation of the motion for transfer. Order for severance and transfer was signed January 14, 1982, with opinion to be filed.

In all, one or another aspect of the case was dealt with by the late Hon. Guy L. Fake, the late Hon. Thomas F. Meaney, the late Hon. Robert Shaw, Senior Judge Lawrence A. Whipple and the writer.

FOOTNOTES

1. For a discussion of the practice of entering an order to be followed by an opinion articulating its basis, see Appendix to opinion in Wolosoff v. Cable Systems, Inc., ___F.Supp.____ (D.N.J. Civ. 80-3388, 4/2/81).

2. The statute for the registration of a judgment entered in one district in other districts, 28 USC §1963, is also applicable here. Registration under the Act is authorized only when the judgment is in an action for the recovery of money or property, which is not the case here. The purpose of the statute obviously is to enable enforcement by writ of execution and the like in any district where it may be satisfied, without the need to file a new suit grounded on the judgment.

Registration under the statute is analogous to the long-establishe system of "docketing" judgments entered in a State court with limited territorial jurisdiction in a higher court with statewide jurisdiction, for both lien and execution purposes. See, e.g., N.J.S.A. 2A:16-32 et seq., providing for the docketing in the Superior Court (which has statewide jurisdiction) of judgments entered in a county district court (which has county-wide jurisdiction).

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY
Civ. 17-49

UNITED STATES OF AMERICA — Plaintiff

vs.

WESTERN ELECTRIC COMPANY, INCORPORATED and AMERICAN TELEPHONE AND TELEGRAPH COMPANY — Defendants.

ORDER CORRECTING TRANSCRIPT

After review of the transcript of the hearing of January 11, 1982, it is, on this 20th day of January, 1982 ORDERED that the following corrections of typographical errors be noted:

Page	Line	Item
2	7	Delete "to", substitute "for"
4	17	After "agreement" delete comma and insert "for"
5	9	Delete "Sentate" and substitute "Senate"
5	19	After "arise", change comma to period and capitalize "Long"
5	25	Delete "and" and substitute "under"
7	25	After "revenues" insert "to a BOC"
7	25	Delete "acts as" and substitute "access"
8	1	Delete "inner exchange" and substitute "interexchange"
8	1	Delete period and insert "of Boc: or AT&T""
8	2	After "that" insert "in"
8	6	Delete "POC" and substitute "BOC"
8	15	Delete "POCs" and substitute "BOCs"
8	23	Delete "date" and substitute "data"
9	3	Delete "redown" and substitute "redound"
9	24	Delete "that"
10	5	Delete "base" and substitute "business"
10	20	After "switchboard" insert "which"
11	2	Delete entire line
11	14	Delete "principal" and substitute "principle"
11	25	After "what", insert "he"
12	8	After "distance" change comma to period and capitalize "It"
13	8	Delete "devises" and substitute "derives"
13	8	Delete "inner exchange" and substitute "Interexchange"
13	14	After "situations", insert comma and change "to" to "too,"
14	13	Delete "bank" and substitute "band"
17	7	After "phrasing" insert comma
18	2	Delete "and sent" and substitute "absent"
18	21	After "anything" insert comma
18	22	After "parties" insert comma

s/ Vincent P. Biunno, USDJ

Original to Clerk
xc: All counsel
Hon. Harold H. Greene

EXHIBIT 17

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

FILED

JAN 21 1982

JAMES F. DAVEY, Clerk

UNITED STATES OF AMERICA, Plaintiff, v. AMERICAN TELEPHONE AND TELEGRAPH COMPANY; WESTERN ELECTRIC COMPANY, INC.; AND BELL TELEPHONE LABORATORIES, INC., Defendants.	Civil Action No. 74-1698
UNITED STATES OF AMERICA, Plaintiff, v. WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE & TELEGRAPH COMPANY, Defendants.	Civil Action No. 82-0192

ORDER

It appearing that Civil Action No. 17-49, United States v. Western Electric Co., et al., was transferred from the District Court for the District of New Jersey to this Court;[1/] it appearing that the parties to Civil Action No. 74-1698, United States v. American Telephone & Telegraph Co., et al., who are also parties to the Western Electric action, have suggested that the Court apply the substantive procedures required by the Antitrust Procedures and Penalties Act, 15 U.S.C. §§ 16(b)-(h) (also known as the Tunney Act) with respect to their settlement of these

1/ That case has been docketed in this Court under Civil No. 82-0192. One segment of the Western Electric action is still pending before the United States Court of Appeals for the Third Circuit. This Court has been advised that motions have been filed to dismiss the appeal and to remand the case to the District Court for the District of New Jersey, and Judge Biunno of the District Court has indicated that, should there be a remand, that remaining segment would likewise be transferred to this Court.

actions;[2] it appearing that, in view of this request, is not necessary that a decision be made at this time whether the Tunney Act applies also as a technical matter;[3] it appearing that the Tunney Act presupposes that a judgment will be entered only after the completion of the procedures required by that statute; and it appearing that a number of entities, both governmental and private,[4] have sought to intervene in these actions to urge the application of the Tunney Act to this settlement, but it further appearing that under the procedure established herein the applicants for intervention will have a full opportunity to comment on the proposed settlement and that intervention is therefore unnecessary; it is this 21st day of January, 1982, in response to the request of the parties, in the exercise of the Court's equitable

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2/ See Memorandum in Connection with Stipulation and Modification of Final Judgment filed in No. 17-49; letters from the parties to the Court dated January 18, 1982; statement of counsel for the parties in No. 74-1698 on January 12, 1982 (Tr. 25,016-26).

3/ For a variety of reasons -- including certainty with respect to any judgment entered herein, confidence in the judicial process, and compliance with Congress' mandate -- it is essential that substantively there be no deviation from the Tunney Act procedures. However, in view of the parties' position that they intend the Act's procedures to be applicable, it is neither necessary to render a decision on the technical applicability of the Act nor appropriate to do so, particularly since such a decision might have collateral consequences -- e.g., an impact on the government's interest in avoiding prejudice to its position in other courts regarding the application of the Act to consent decree modifications or on the possible interest of defendants with respect to liability in private antitrust actions -- which are beyond the Court's concern in these proceedings at this time.

4/ The following have sought to intervene as of the date of this order: State of California and the Public Utilities Commission of the State of California; State of Michigan and the Michigan Public Service Commission; State of New York, the New York State Consumer Protection Board, and the Public Service Commission of the State of New York; the Public Advocate of New Jersey; Consumer Counsel of Ohio; Nat'l Ass'n of State Consumer Advocates; the States of Maine, Alabama, Arizona, Colorado, Idaho, Illinois, Iowa, Louisiana, Maryland, Massachusetts, Minnesota, Montana, New Hampshire, New Mexico, North Dakota, Oregon, Rhode Island, Tennessee, Texas, Utah, Vermont, Washington, West Virginia, Wyoming; Alarm Industry Telecommunications Committee of the Nat'l Burgler & Fire Alarm Ass'n; Computer and Communications Industry Ass'n; Independent Data Communications Manufacturers Ass'n; Jack Faucett Associates, Inc.; MCI Communications Corp.; North American Telephone Ass'n; Southern Pacific Communications Co.; Nat'l Ass'n of Regulatory Utility Commissioners; Tandy Corp.; and U.S. Telephone Communications, Inc.

powers,[5/] and in order that the public interest proceedings be conducted in a concrete framework and pursuant to an orderly, well-defined procedure,

ORDERED as follows:

1. Civil Action No. 74-1698, United States v. American Telephone and Telegraph Company, et al., and Civil Action No. 82-0192, United States v. Western Electric Company, et al., are hereby consolidated for the conduct of the procedures set out below;

2. The Order entered on January 11, 1982, approving the modification of final judgment in United States v. Western Electric is hereby vacated;

3. The Modification of Final Judgment and the Stipulation for Voluntary Dismissal (hereinafter collectively referred to as the proposal) filed in Civil Action No. 17-49 and lodged in Civil Action No. 74-1698 respectively, on January 8, 1982, shall be published by the United States in the Federal Register as soon as practicable.

4. Within fifteen days of the entry of this order, the United States shall file with this Court, publish in the Federal Register, and thereafter furnish to any person upon request, a competitive impact statement which shall recite --

(1) the nature and purpose of the proceeding;

(2) a description of the practices or events giving rise to the alleged violation of the antitrust laws;

(3) an explanation of the proposal, including an explanation of any unusual circumstances giving rise to the proposal or any provision contained therein, relief to be obtained thereby, and the anticipated effects on competition of such relief;

5/ See, e.g., United States v. Swift & Co., 1975-1 Trade Cas. ¶60,201 (N.D. Ill. 1975); United States v. Ling-Temco-Vought, Inc., 1970 Trade Cas. ¶73,156 (W.D. Pa. 1970); United States v. F. & M. Schaefer Brewing Co., 1968 Trade Cas. ¶72,345 (E.D.N.Y. 1967); United States v. Carter Products, Inc., 211 F. Supp. 144 (S.D.N.Y. 1962).

(4) the remedies available to potential private plaintiffs damaged by the alleged violation in the event that the Modification of Final Judgment and the Dismissal are entered in these proceedings;

(5) a description of the procedures available for modification of the proposal; and

(6) a description and evaluation of alternatives to the proposal actually considered by the United States.

5. Within fifteen days of the entry of this order, the United States shall make available to the public at this Court, the District Court for the District of New Jersey, and the district courts listed in the Appendix to this order, copies of the proposal and of any other materials and documents which the United States considered determinative in formulating the proposal.

6. Any written comments relating to the proposal received by the United States within sixty days after the filing by the United States of the competitive impact statement required by paragraph 4 of this order (or within such additional period as may be allowed under paragraph 8 of this order), and any responses by the United States thereto, shall be filed with this Court and published by the United States in the Federal Register not later than fifteen days after the close of the comment period provided for under paragraph 8.

7. The United States shall cause to be published, commencing within fifteen days from the date of this order, for seven days over a period of two weeks, in newspapers of general circulation in the District of Columbia, the District of New Jersey, and the districts listed in the Appendix to this order --

(1) a summary of the terms of the proposal;

(2) a summary of the competitive impact statement filed under paragraph 4 of this order;

(3) a list of the materials and documents under paragraph 5 of this order which the United States shall make available for purposes of meaningful public comment, and the

place where such materials and documents are available for public inspection; and

(4) directions for the submission to the United States of written comments relating to the proposal.

8. During the sixty-day period specified in paragraph 6, of this order, and such additional time as the United States may request and the Court may grant, and pursuant to 28 C.F.R. § 50.13 or such other procedures as may be established by the Attorney General or his designee, the United States shall receive and consider any written comments relating to the proposal. Such comments and the response of the United States shall be filed and published as required in paragraph 6 of this order.

9. Before entering the Modification of Final Judgment in Civil Action No. 82-0192 and the dismissal in Civil Action No. 74-1698, the Court will determine whether the entry of judgment in these cases is in the public interest. For the purpose of such determination, the Court may consider --

(1) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration or relief sought, anticipated effects of alternative remedies actually considered, and any other considerations bearing upon the adequacy of such judgment; and

(2) the impact of entry of such judgment upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of the public benefit, if any, to be derived from a determination of the issues at trial.

10. In making its determination under paragraph 9 of this order, the Court may --

(1) take testimony of government officials or experts or such other expert witnesses, upon motion of any party or participant or upon its own motion, as the Court may deem appropriate;

(2) appoint a special master and such outside consultants or expert witnesses as the court may deem appropriate; and request and obtain the views, evaluations, or advice of any individual, group or agency of government with respect to any aspects of the proposal or the effect of the judgment, in such manner as the Court deems appropriate;

(3) authorize full or limited participation in proceedings before the Court by interested persons or agencies, including appearance amicus curiae, intervention as a party pursuant to the Federal Rules of Civil Procedure, examination of witnesses or documentary materials, or participation in any other manner and extent which serves the public interest as the Court may deem appropriate;

(4) review any comments including any objections filed with the United States under paragraph 8 of this order concerning the proposal and the responses of the United States to such comments and objections; and

(5) take such other action in the public interest as the Court may deem appropriate.

The Court will decide at a later date which of these procedures will actually be applied with respect to these cases.

11. Within fifteen days of the entry of this order, the defendants shall file with the Court a description of any and all written or oral communications by or on behalf of such defendant or defendants, including any and all written or oral communications on behalf of such defendant, or other person, with any officer or employee of the United States concerning or relevant to such proposal, except that any such communications made by counsel of record alone with the Attorney General or the employees of the Department of Justice alone shall be excluded from the requirements of this subsection. Prior to the entry of judgment herein, the defendants shall certify to the Court that the requirements of this paragraph have been complied with and that

such filing is a true and complete description of such communications known to the defendant or which the defendant reasonably should have known.

12. In accordance with 15 U.S.C. § 16(h), proceedings before this Court under paragraphs 9 and 10 of this order and the competitive impact statement filed under paragraph 4 of this order shall not be admissible against any defendant in any action or proceeding brought by any other party against such defendant under the antitrust laws or by the United States under 15 U.S.C. § 15a nor constitute a basis for the introduction of the consent judgment as prima facie evidence against such defendant in any such action or proceeding.

13. Within five days of the date of this order, the parties may move for modification of the districts specified in the Appendix hereto and of the time limits established in this order. The sixty-day time limit provided for in paragraphs 6 and 8 will be shortened by order of this Court upon a showing that (1) extraordinary circumstances require such shortening and (2) such shortening is not adverse to the public interest.

14. All motions currently pending before the Court to intervene or to participate as amicus curiae are hereby denied, without prejudice to the rights of the movants to submit comments and otherwise to participate in the proceedings required to be held pursuant to this order.

Harold H. Greene
United States District Judge

APPENDIX */

Central District of California

Northern District of California

Southern District of California

District of Colorado

Middle District of Florida

Southern District of Florida

Northern District of Georgia

Northern District of Illinois

Eastern District of Louisiana

District of Maryland

District of Massachusetts

Eastern District of Michigan

District of Minnesota

Eastern District of Missouri

Southern District of New York

Northern District of Ohio

Southern District of Ohio

Eastern District of Pennsylvania

Western District of Pennsylvania

Northern District of Texas

Southern District of Texas

Eastern District of Virginia

Western District of Washington

Eastern District of Wisconsin

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*/ These district courts are located in the largest metropolitan areas of the United States. To achieve a wider geographical balance, district courts located close to the eleven U.S. Courts of Appeals have also been included.

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